AN ECONOMIC INTERPRETATION OF INVESTMENT

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PREFACE.

The object of these chapters, some of which were published in the "Financial Review of Reviews" during the autumn of 1910, is to present a study of the art of investment upon its industrial, rather than its financial, side, that is to say, to consider it in relation to the productive energy it develops, directs, organises, and utilises. For while it is evident that investments cannot normally fulfil any of their financial functions, as repositories of savings, instruments for enhancing capital-values, and for earning dividends, without doing actual work, investors do not, as a rule, trouble themselves sufficiently to understand what the work is, and how it is performed.

This insufficient attention to the industrial side of financial investments is a source of error and of actual danger to the art of investment. For it leads to excesses and defects of expectation which could be corrected by closer consideration of the industrial facts and forces upon which the values of financial securities in the long run rest.

The art of finance, divorced from the solid facts of business life, is apt to trust too much to the rule of chance or the miraculous.

In a brief sketch of the origin of joint-stock enterprise, I have endeavoured to trace its rise and growth for the actual needs of modern manufacture and commerce under the pressure of the mechanical and other technical improvements of the productive arts, commonly summarised under the term Industrial Revolution. Investment is thus realised as the process of the distribution of productive energy over an ever-widening area of activity, the movement of capital which it primarily effects being accompanied by a corresponding flow of business ability and labour-power, to co-operate with concrete capital in the production of wealth.

After a short study of the machinery by which this distribution of industrial power is effected, and the chief modes of waste to which it is exposed, I proceed to a consideration of the extent to which the various countries of the earth are engaged in forwarding this process, as lenders or as borrowers, and the economic forces which determine their financial conduct.

The most striking phenomenon of modern economic life is the rapidly-growing internationalisation of capital in its operation through Joint-Stock Companies and governmental investments. Important political implications can be traced

to this growth of extra-national ownership, by which, for example, a number of British citizens possess and operate a great part of the productive capital in Argentina. The larger processes underlying these modern tendencies of finance are the economic standardisation and co-operation of the civilised world, as the material basis of civilisation is extended to the more backward countries, first, through railways and other modes of communication, then through developmental processes applied to mining, city structures, and agriculture, lastly through the fuller industrial life of manufactures and trade.

In a final chapter of a more speculative kind, the probable future of the general process of investment is discussed in the light of modern economic and social movements.

J. A. HOBSON.

May, 1911.

CHAPTER I

ORIGIN OF JOINT-STOCK ENTERPRISE.

NEITHER investors nor the operators of financial machinery are wont to give any close or continuous attention to the industrial or other economic work done by the capital with which they are concerned. They are primarily and almost exclusively occupied with the monetary value and the monetary yield of the stocks and bonds which from their standpoint constitute capital. Indeed, many of the more speculative processes of finance are still further removed from industrial reality, being concerned, as it were, with the shadows of these monetary forms, the mere names or images of stocks and shares. Even the genuine investor, regarding his investments as a store of wealth and as a means of income, is seldom able, even if he has the desire, to realise, in any clear or detailed manner, the concrete capital that corresponds to the paper certificate he holds, or the concrete services it renders in the production of wealth. Indeed, the whole tendency of the modern evolu-

Light in which the average Investor views his Capital.

tion of the art and instruments of investment is, by widening the distance between the ownership and the economic operation of capital, and by increasing the elaboration of capitalistic processes, to remove the legal owners of ships, steam engines, factory plant, merchandise, and other joint-stock property from the possibility of exercising any direct personal control over their property.

Early investment methods.

Foundation of modern capitalism.

In earlier times, before the era of modern capitalism, a man who saved would put his savings into some piece of land or house property in his immediate neighbourhood, or would employ it in his own business, or else would loan it to some man he knew for some specific purpose, taking a pledge the worth of which he could personally estimate and watch. The ownership of the tools, premises, materials, etc., which constituted the capital of a business, was nearly always within the compass of a single family, and the usual, indeed, the sole avenue for useful employment of savings was within this business Except for rare enterprises, open to very few, there was no opportunity or use for joint-stock capital, and no possible or reasonably safe employment for it beyond the eyesight of its owner. The early roots of modern capitalism, doubtless, are traceable far back in the single ventures of groups of merchants who fitted out vessels for the hazards of over-seas trade, and in the goldsmiths and other money-lenders who became the repositories of such spare treasures as, having no immediate use at hand,

were available for loans to princes or to nobles. The former practice, laying the foundations of the "regulated" and afterwards the joint-stock companies, such as the East India or the Turkey Company, which in the seventeenth century came to monopolise large sections of foreign trade and to establish "factories" and other permanent trading stations on foreign shores, may be regarded as the true prototype of the modern form of productive business, as the latter was of our system of banking, insurance, and finance.

Early joint-stock operations.

But the actual part played by such joint-stock operations was trivial in importance, and, with rare exceptions, meagre in results. The eighteenth century, with all its beginnings of industrial revolution, afforded no intimation of the swift growth of the new financial structure which a few generations were destined to achieve. Early in that century the amazing gamble of the *South Sea Bubble* discredited the progress of the foreign trading company, and though the scope for employment of capital in home trade and manufacture, and in the provision of the new wants of growing cities, had greatly enlarged, no serious endeavour was made to furnish and apply this capital by co-operative enterprise. Legal difficulties stood in the way.

The "Bubble Act" of 1719.

The "Bubble Act" of 1719 prohibited the formation of companies with *transferable shares*, unless they obtained incorporation by royal charter or by special Act of Parliament. While this prohibition was imposed for the protection of the public, there is no reason

to suppose that business men or economists were alive to the important future of joint-stock investment. Adam Smith's famous pronouncement may be taken as a representative judgment of his time. "The only trades which it seems possible for a joint-stock company to carry on successfully, without an exclusive monopoly, are those of which the operations are capable of being reduced to what is called a routine, or to such a uniformity of method as admits of little or of no variation. Of this kind, is, first, the banking trade; secondly, the trade of insurance from fire and from sea risk and capture in time of war; thirdly, the trade of making and maintaining a navigable cut or canal; and, fourthly, the similar trade of bringing water for the supply of a great city." * This classic utterance is as remarkable for its acuteness in summarising known facts and tendencies as for its blindness regarding the new forces of the industrial revolution. Banking, Insurance, Transport and Municipal Services, the development of the four sorts of enterprise he names, have passed more completely than any other trades into the form of joint-stock investments either as companies or as public undertakings. What neither Adam Smith nor anyone else of his time foresaw was the miraculous and swift transformation which mechanical inventions and steam-power could bring about in the arts of manufactures, bringing larger and larger sections of ordinary industry under that economy of "routine" which

Adam Smith on joint-stock possibilities.

Industrial revolution the path to joint-stock enterprise.

* "The Wealth of Nations," Book V., Ch. 1, Part III.

he rightly regarded as a prime condition of successful joint-stock enterprise.

The beginnings of the modern factory system in Great Britain thus arose outside the Company system, by a wasteful, hazardous, and inconvenient method of finance, in which banks and other loan agencies found capital for the energetic mill-managers who built up the mills of Lancashire and the West Riding. But the close of the first quarter of the century was signalised by a premature and short-lived attempt to force joint-stock capitalism before an adequate legal and financial machinery had been established.

Premature joint-stock enterprise

An interesting list of the projects of 1824 and 1825, showing the economic quarters from which the pressure for a new finance was proceeding, is given by Mr. Gilbart.*

Joint-Stock Companies of early 19th century.

		Capital.
74	Mining Companies...	£38,370,000
29	Gas do.	12,077,000
20	Insurance do. ...	35,820,000
29	Investments do. ...	52,600,000
54	Canal, Rail Rd. do.	44,051,000
67	Steam do.	8,555,500
11	Trading do. ...	10,450,000
26	Building do. ...	13,781,000
24	Provision do. ...	8,360,000
292	Miscellaneous do. ...	148,108,600
626		£372,173,100

* The History and Principles of Banking, p. 57.

Of these companies a large proportion never came into existence, many others were abandoned shortly after birth, and in 1827 only 127 of them were operative, with a paid-up capital of no more than £15,185,950, about one-sixth of the capital required. Very few of them survived beyond a few years.

Foreign loans raised in England between 1821 and 1832.

About this time, also, large numbers of foreign loans were financed in England by London bankers, the total sum between 1821 and 1832 amounting to about fifty-five millions. Most of the leading countries of Europe figure in the list of borrowers, together with a number of South American States, though Brazil alone among the latter maintained the payment of the dividends.

Joint-stock legislative measures.

The panic of 1825, and the collapse of credit following this burst of speculation, brought about legislative changes favourable to security and enterprise of joint-stock capital. The Bubble Act was repealed in 1825, greater liberty being accorded to the incorporation of joint-stock trading companies. In 1844 further legislation simplified and cheapened the process of incorporation, but it was not till 1862 that the consolidation of the new Companies Acts effectively established the principle of limited liability which is essential to the full economic efficacy of joint-stock investment.

It is important to recognise the definite modes of economic pressure which broke down the legal barriers and moulded the new business structure. Though the moderate capital required for an early

cotton mill or foundry could be found without resort to an investing public, this was not the case when the great organization of the mining industry, which was the material foundation of the new economic order, was taken in hand. The money for such vast and speculative enterprises could only be found by expanding the area of collection; the early drains upon the Banks and other restricted avenues of finance were productive of continual alarms and crises. Of equal importance was the need for a free flow of savings to develop as rapidly as possible the new steam-transport by land and sea requisite to secure and to supply new markets for the products of our mines and factories; and to bring in and distribute the materials and foods required for the growing population of our towns. In 1840 the first joint-stock company was formed to provide a service of steamers between London and Bombay, and the forties and fifties saw the establishment of a complete railroad system and steamer services to the chief trading centres of the world on a basis of joint-stock investment. As the new mode of sea-transport opened up large distant markets for the products of British factories, and at the same time drew upon British savings for the railroad and mining development of foreign countries, especially in North and South America, the inadequacy of our banking and monetary system to meet the new demands became apparent. The monopoly of the Bank of England and its antiquated policy in regulating credit were no longer

The first Joint-Stock Steamship Co.

Joint-Stock Capitalisation: inadequacy of the Banking System.

to be tolerated. After 1825 joint-stock banking companies were permitted to struggle into being, but not until the Bank Charter Act of 1844 did they enjoy the facilities requisite for success. Even after that they owed their profitable development mainly to the fact that the right of issuing notes, which Sir Robert Peel sought to secure as a monopoly for the Bank of England, became relatively unimportant in view of the unanticipated growth of the use of cheques for most purposes of purchase. Though the new bank policy was subjected to a terrible strain for several years, the central responsibility thrown upon the Bank of England of keeping an adequate reserve, coupled with the encouragement of rival banking establishments, contributed greatly to establish confidence in the saving classes and to assist in collecting and directing into joint-stock investments the large and growing surplus of the new industrialism.

Birth and progress of Joint-Stock Banking.

It is no part of my purpose to describe in detail the manifold or complicated structure which forms the framework to the process of investment, drawing the new stream of free capital into definite channels of employment and securing facile transfer of ownership for the bonds and shares which are its financial equivalents.

Framework of investment.

The creation of new forms of investment involves various sorts of skill and enterprise in classes of financial middlemen, varying with the nature of the investment. When public loans are issued by States or Municipalities, bankers,

brokers, or other financial agents usually make the issue, sometimes purchasing the whole issue and undertaking the risk of placing it, sometimes acting merely as an agent. Where a new company is to be floated, either by the capitalisation of an existing business or businesses, or by the creation of a business to exploit a new proposition, nicer qualities of skill and judgment are required. There is a call for specialists of two sorts. First, a class of experts in profitable notions is needed, men who can select, out of the countless proposals which business men, inventors, and prospectors, bring forward for consideration, those which can be made to pay. Though a paying proposition from this standpoint means one capable of being recommended to an investing public so as to evoke the subscription of capital, and does not necessarily imply a sound productive enterprise, such expert judgment is indispensable, and, after due allowance for merely specious or even fraudulent representations, involves a really serviceable skill of a high intellectual order. But the promoter is not merely a man with an eye for profitable ideas. He must know how to present them to the investing public. Here comes the special art of the Prospectus. Like other tradesmen, he must know how to dress a shop window, how to present his goods in their most attractive guise, and to conceal any defects. He has to study on the one hand the psychology of the investor, on the other the conditions of Company Acts which seek to limit his liberty of statement or concealment.

Floating a company: the *modus operandi*.

Qualifications of the expert Prospectus writer.

Here he enjoys perhaps to an unusual extent the advantage which the expert possesses in dealing with the amateur, for whereas the goods which most advertisers sell can be tested on delivery, the purchaser of stocks and shares is often liable to be deceived for some time as to the real merits of what he has bought.

The important part played by middlemen.

But, however large the allowance to be made for fraud and overreaching on the part of skilled middlemen, the delicacy and importance of the services they render, in bridging over the wide gulf between the individual act of saving and the supply of co-operative masses of concrete capital for innumerable great enterprises all over the world, are undeniable. A delay of half a century in the development of a whole country as big and as rich as Great Britain, or the fate of a whole series of industrial inventions, may sometimes hinge upon the exact selection of time and method in the issue of a prospectus, the names of the directors, the nature of the information given or withheld, the apportionment of the capital assigned to different classes of bonds or shares, or any one of a series of such determinant details.

Produce and Investment markets: a comparison.

The evolution of the structure of the market for securities is of no less importance. Most markets for material goods, whether foods and raw materials, manufactured wares, implements of production, or real estate, are immediately confined within local limits, and the causes which affect their values are more or less ascertainable

and calculable. This is even true to some extent of articles such as wheat, raw cotton, copper, etc. which have a world market. But the markets for large classes of securities, though ultimately rooted in concrete industrial facts, are far more sensitive and incalculable. For large orders of securities are in wider demand, more divisible, more transferable, and so more immediately negotiable than any sort of actual produce, while the markets for different sorts of securities are more closely and strongly interactive and sympathetic than the markets for concrete goods. Thus the buying and selling of stocks and shares is a more intricate art than other sorts of dealing. The intangible, extremely sensitive, and variable nature of these "goods" requires a *trained profession of skilled advisers* to assist the necessarily unskilled investor to place his savings safely and profitably. For published price-lists only communicate some of the material facts, and the knowledge of current prices in relation to the yield of stocks is a very insufficient guide to purchasers who do not know, either the economic facts affecting the probable future of these stocks, or the artificial or casual operations in the world of finance which may have brought about some temporary rise or fall in a particular stock. Experienced and reliable brokers have thus a *raison d'être* in the financial system, not as mere middlemen to perform the acts of buying and selling, but as professional advisers in the matter of investment. While improvements in stock

The investor's need for professional advice.

Pitfalls for the inexperienced investor.

market reports, and better financial education in the investing classes, may reduce the importance of this advisory function, they cannot wholly dispense with it even in the case of gilt-edged securities and other widely marketable shares. Moreover, there will always remain large numbers of local and other less known securities, the market price of which is not published or easily ascertainable, where not merely advice but skilled bargaining is requisite.

The magnitude of the Investment Market.

The mere intricacy and magnitude of an investment market which includes every variety of Government and municipal security, railroad, mining, industrial, and financial companies of every sort and size, and every degree of market area, introduce into stock-broking a division of labour finer than in any other sort of marketing. Hence it has arisen that dealing in stocks, originally confined, almost entirely, to a market which took place in the Bank of England itself, found it necessary to set up as a separate institution under the title of the London Stock Exchange, with a fission between jobbers and brokers, and a continually increasing specialisation of the classes of investment to which jobbers confine themselves. This closely-regulated private club in London has been imitated in its structure by provincial Stock Exchanges, dealing mainly with companies which represent local industries and municipal stocks. The close monopoly of these Stock Exchanges has given rise to a large growth of outside brokers who do an increasing share of the buying and selling

The origin of the London Stock Exchange.

both for investment and for speculation.

Though London is the great world-centre for this market, the machinery of Stock Exchanges extends throughout the commercial capitals of every civilised country, the methods of business in most countries being usually more free than in the London Stock Exchange. These Exchanges, and the price-lists which register their dealings, are in such close and constant communication as to maintain, at any rate for large masses of securities, the conditions of a world-market, though national and even local causes will often bring about considerable temporary, and sometimes durable, differences of prices for the same "goods" in several financial centres. Considerations of patriotism, local knowledge, preferences resting upon particular habits or temperaments, will affect to some extent the prices even of securities which figure in the world-market. But within these limits, which continually tend to grow narrower, the elaborate system of cosmopolitan finance tends to level prices for an ever larger number of securities. Interpreted in terms of concrete economics, this means that the investment mechanism becomes better and better adjusted to perform its essential task, viz., that of distributing real capital so as to make it function most productively in the exploitation of the natural resources and labour power of the world.

The ramifications of the Stock and Share market.

Duties performed by Stock Exchanges.

CHAPTER II

HOW FINANCIAL CAPITAL DOES ITS WORK.

INVESTMENT is not an Art for Art's sake. It has come into being and exists to promote industrial ends, to assist in producing and distributing actual concrete wealth. This, the essential and the social meaning of Investment, is indeed so remote from the thoughts of most investors as to require further enforcement before it is accepted. They are apt to live in a monetary world of paper values, which comes almost to acquire a separate existence of its own; for though their stocks or bonds may have reference to some concrete forms of wealth—some railway or some factory plant—they need not have any such material embodiment. They may be Consols or some other form of public indebtedness, which seems to have no support in actual economic capital. Or, when there are material forms behind the paper certificates the investor has never seen, and so cannot adequately realise, them. Moreover, the fluctuations in the value and the yield of his paper, which are his real concern, usually appear to occur without any corresponding

The *raison d'être* of Investment.

change in the plant, land, machines, buildings, or other real wealth said to underlie it. Where some happening in the industrial world, some famine, strike, new invention, does visibly affect the value of his investment, it usually comes as an unexpected stroke of fortune or misfortune rather than as a normal factor in the art of investment.

The superficial interest of the investor.

Most of those who bring real skill and knowledge to the choice and management of their investments confine their study and their reasoning to the financial and statistical evidence, not seeking to investigate, as indeed they are seldom competent to do, the economic facts and forces which are the material basis of the statistics. If the ordinary investor thus realises so slightly, and concerns himself so little with, the concrete capital and the real economic processes which vitalise his investment, still less is he likely to realise the wider social significance of the process of investment in general as a function of the economic system of the world. Yet I venture to claim that a comprehension of this larger meaning of investment, as an instrument for forwarding the production and distribution of world-wealth, not merely possesses a scientific interest, but has important practical implications. For by establishing clearer relations between financial values and economic utilities, it helps to steady and direct the judgment regarding the substance and stability of present investments and the probabilities of the investing future.

Investment process a function of the world's economic system.

Earning power of invested capital.

The validity of investment rests in the earning power of capital. Now capital, like labour, can only earn by working. How does invested capital work? Money in itself, as Moses and Aristotle recognised, is barren, and an investment which simply meant a transfer of credit from the investor's bank account to the account of a company issuing bonds or shares, would not seem to be an economically useful act. But bank credit, or any other money, gives its owner a command over the whole stock of goods and services existing for sale throughout the world, proportionate to its amount. Not only by applying it in a particular direction can he get possession of any sort of tangible wealth that exists, but, by announcing his intention to apply it in a particular way, he can so stimulate and direct the industrial forces of the world as to bring into existence any sort of wealth he wants. It is, of course, this general command over productive energy which the investor transfers to the new Company whose share capital or debentures he purchases. Subscribing the original capital of a new railway in Argentina, or a mine in the Transvaal, means, so far as the company is a genuine business proposition, the issue of orders which secure the requisite control of land or other natural resources, evoke the productive activity of plant and labour in the engineering, steel-making, and other trades that supply plant and other apparatus for the railroad or the mine, for the conveyance of these requisites

How the investor directs the world's Industrial Forces.

to the place where they are wanted, and for the collection and transport of the various sorts of labour required to make and operate the railway or the mine.

This is the primary economic meaning of all investment, viz., to determine the distribution of economic energy over the various industries and localities so as to produce the largest amount of marketable goods and services. Investment is the great dynamic instrument of the economic system. A statical view of an industry seems to show it as consisting in a complicated structure of specialised and localised forms of plant, buildings, materials, labour, engaged in more or less regular routine processes, and incapable, except at great loss, of being adapted to produce other goods, or to shift its place of operation. But this appearance of stability and specialisation is very illusory. All the time large quantities of "free" capital in the form of savings, and of "free" labour in the form of young adult humanity, are ripening for economic use. Moreover, the stability of the existing forms of business-structure, the mines, factories, machinery, railways, ships, warehouses, etc., is only secured by a continuous stream of new productive energy applied to the work of replacement and repair. All this is done by adapting and directing the fresh flow of free energy stored in the minds and bodies of men and the new supplies of material informed by this energy. Not only are new large business operations, involving the application of fresh stores of capital

Scientific meaning of investment.

Statical view of industry an illusion.

and labour, constantly coming into being, but old operations becoming obsolete, or relatively useless and unprofitable, are being let down and are passing into decay. So the transformation of the industrial and commercial structure of the world, the growth and decline of whole trades, or their transfer from one place to another, the development of fresh natural resources and new manufacturing countries, proceed far more rapidly than at first seems possible.

Life of modern machinery decreasing.

The actual life of modern machinery and business buildings, and of most other forms of "fixed" capital, becomes continually shorter and more intense, i.e., it gives out its productive use at a faster pace. Consider the pace of the structural changes in the business portions of such great cities as New York, Berlin, or London, the scrapping of expensive machinery that goes on in the more developed manufacturing industries, the flood of industrial energy which is spent in fitting new cities with a body of steel and a soul of electricity. Practically the whole of the concrete capital structure of the modern world, with the exception of the more primitive roads, buildings, and earlier agricultural developments, have been the product of the "savings" of the last few years. Though by no means the whole of such saving has passed through the machinery of investment with which we are here concerned, an ever increasing proportion is thus furnished. Financial capital, provided through joint-stock companies, is now the

Concrete capital structure produced by "savings."

great fertilising stream in world-industry. The extension of banking facilities, of stock exchanges and investment agencies of various orders, with the ever-growing publicity of the press and of telegraphic facilities for communication of news and transfer of payments, feed this stream by an ever increasing number of little rivulets of savings, and distribute it over an ever wider area of the world's surface with an increasing rapidity and accuracy of adjustment. For the whole economic purpose of this elaborate instrument of investment is to apply concrete capital and labour-power of requisite amounts and qualities at various points of the industrial world, so as to develop and utilise natural resources and opportunities. What is thus distributed is not (save to a very small extent) the "money" which savers and investors have subscribed, it is the plant, machines, stock and other material equipment together with the brain and muscular power for operating them that are thus distributed.

Joint-stock capital the food of world-industry.

With certain qualifications and partial exceptions to this industrial interpretation of investment I will deal presently. It is important first to grasp securely this central truth about the meaning of investment. The economic function of investment is to send concrete capital tapping every corner of the earth to find out where it can find natural resources and labour for profitable exploitation. In proportion as this function is skilfully fulfilled the wealth of the world is increased, and though the primary object of the

Economic mission performed by investment.

owners or operators of each portion of this invested capital is to raise the selling value of their shares and the yield in dividends, they are usually compelled by competition to communicate a good deal of the gain of their proceedings, through normal processes of markets, to other people in their capacity of consumers or producers.

Such is the general rationale of the art of investment regarded from the social-economic standpoint. To many practical financiers it will appear a somewhat idealised picture of what really takes place when an issue of bonds or shares occurs. It assumes, first, that all the capital subscribed is represented in the economic world by railroad or mining plant, or rolling mills, or even rubber trees, concrete forms of material capital engaged in producing the various forms of wealth the profit on the sales of which is paid as interest and dividends. Now a great proportion of invested capital is not represented in the economic world by any tangible assets. Much of it is represented by state or municipal indebtedness. A government may finance a war by raising a loan, that is to say, it may ask investors to supply capital not in the form of harbours, public buildings, roads, or other productive instruments, but in the form of guns, ammunition, stores, etc., or other "consumables" to be destroyed or used up in a campaign. When the campaign is over, there appears nothing left of the subscribed capital, except the obligation of the State to raise taxes so as to pay the annual interest. It appears to be identical

Capital not represented by tangible assets.

Government loans for war purposes.

with the case of a loan made by a money-lender to a spendthrift, save that the money-lender gets security in the shape of some tangible property. In neither case does it appear as if the investment were attended by any real saving in the shape of new forms of capital; the saving of one party has been attended by an increased spending of the other.

Capital for Pyrotechnics.

Consols appear to be the most obvious illustration of this order of investment which has no productive assets behind it, representing mere indebtedness. But a large proportion of national debts are of the same order, appearing to represent mere public extravagance. The "capital" has been converted into fire-works which have been "let off." This *prima facie* judgment, however, demands revision. We are not entitled to assume that all expenditure on armaments and wars is in the broader economic sense "unproductive," and that, because it leaves behind no tangible assets, it is entirely unrepresented in the economic world. Take the example of a defensive war to repel an attack which threatened grave damage to our coasts or to our trading interests; or an offensive war to acquire new markets, or to develop the natural resources of a backward country. Unless we hold that all wars have been necessarily "bad business" from the standpoint of both parties, we cannot assume that no genuine though intangible assets in the shape of security, trade routes, goodwill, etc., represent the war expenditure.

Representation of war loans.

Though the uneconomic motives and methods which attend most expenditure on war may induce the belief that most of such expenditure is sheer waste, or even worse, an incitement to more waste, a steady economic analysis will not permit us to place in this category the whole of the public debts attributable to such expenditure. A necessary or a useful war, economically conducted, might, at any rate from the standpoint of the nation, be regarded as a productive expenditure of capital, *and this capital must be considered to survive in forms corresponding to good-will in a private business. Though much of this intangible national capital, consisting in liens upon certain trading advantages or other competitive gains, may be offset in the balance-sheet of the world by corresponding losses of other nations, all cannot be written off in this fashion.

War loans a productive expenditure.

While, then, it is impossible to say how much real though intangible assets underlie our National Debt, or the war loans of other countries, we cannot dismiss as economically negligible the national security and other gains such expenditure was undertaken to obtain. As a rule, however, it is true that Government Loans have no "real security" behind them. In some cases the obligation to pay interest may be supported by some special hypothecation, as where the revenue of

Security of Government Loans.

* This qualified judgment as to the possible economic utility of a successful war, applicable to past times, requires further qualifications for the present and the probable future.

Customs or of some monopoly is pledged in payment. But this does not affect the substance of the transaction: the interest is not really earned by the "capital" whose investors or holders it remunerates. That "capital" has either evaporated or is represented by some quite intangible and immeasurable forms of public well-being. While, therefore, strict reasoning obliges us to deny that Consols and other Government Loans are wholly destitute of substance and are merely "notes of hand" backed by a nation's credit, it must be admitted that any economic substance which such "capital" contains is so vague and attenuated that it cannot rank seriously in our account of the "economic work" of investments. Such loans have in effect been the great despoilers of industry, and, by the temptations they present to certain classes of the saving public, the great retarders of industrial development. It has been far too easy for Governments to secure and divert to extravagant or destructive public projects a large portion of those industrial savings needed to promote the full development of world-industry, by promises of interest drawn by taxation from the proceeds of current industry.

Government Loans the enemy of Industrial Development.

Corporation Loans which further Industrial Development.

Very different are those State or Corporation loans which, being utilised in solid works of permanent and fructifying improvement, such as railways, harbours, land reclamation, water works, produce continuously an output of useful services. Whether the interest upon such loans is paid out of the pecuniary yield

of the special services they render, or by some general charge upon the rates or taxes, does not affect the substance of the case: there is "real" capital producing "real" income at the back of such investments.

The theory of financial capital as a fertilising stream is subjected to a severer practical criticism when it is pointed out that no inconsiderable part of the capital invested every year never materialises in any serviceable shape, but simply passes from the pockets of foolish or unfortunate investors into those of unscrupulous or reckless financiers who float bogus companies, or palm off shares, which have slight value, at exaggerated prices. How large a proportion of the invested savings of the public is thus diverted it is idle to conjecture, but probably a considerable percentage of the whole. Though for a time such investments may retain the appearance of capital, having a quoted and even a selling value, the productive wealth they falsely purport to represent has been converted into promoters' and financiers' profits, and has probably been consumed. Masses of such investments are continually being created and disappearing, without performing any sort of economic work, or even assuming shape in capital-goods.

Capital losses of careless investors.

Investments which benefit the company promoter only.

In such analysis, however, proper allowance must be made for two items which are sometimes of dubious validity. These are expenses of flotations and "good-will," under which latter term is sometimes included patents, contracts, copy-

rights, etc. So far as the former is confined to such costs of promoting, underwriting and advertising, as are necessary in putting the business on a sound financial basis, they are economically justifiable and may properly be represented in shares, though there may be no material or strictly productive assets corresponding to these shares. The fact that in not a few cases such shares are unduly multiplied, and may be made the instrument of diverting much of the subscribed capital into the private possession of vendors or promoters, must not lead us to ignore the fact that so long as the financing of businesses runs on present lines, some expenditure of this order is necessary and may even be regarded as productive and therefore rightly represented in share capital.

Representation of Company Promotion expenses.

A similar distinction applies in the case of "good-will." So far as the value of this item of capital is accurately based upon a reasonable valuation of the probable future earning power of the business, it is legitimate to take it into account in estimating the total value of the capital. Its essentially incalculable and speculative character, and the false modes of estimate to which it lends itself for prospectus purposes, are undoubtedly accountable for a vast amount of "water" in the capitalisation of many businesses converted or amalgamated into Companies. But the future earning power, so far as it is rightly ascertainable, is the only scientific basis of capitalisation; though for practical purposes in some sorts of business it may be safer to value the tangible assets separately

Value and earning power of Good-will.

and to make a special allowance for the individual items which go to make up "good-will." If, however, the latter valuation afforded a lower capitalisation than in the opinion of investors was justified by anticipations of the earning power, this discrepancy would of course be reflected in an appreciation of the price of shares, those who were allotted shares at par receiving a bonus representing the difference between the formal and the actual valuation of the capital. How far "earning power" can rightly be interpreted as commensurate with industrial service or productivity of capital in the sense of our present inquiry, is quite another question. Its answer depends upon how far the future earning power derives from the possession or use of some monopoly or scarcity, how far from the possession of some really productive economic power. A high earning-power derived from an amalgamation of competing firms, which now that effective competition disappears will be able to maintain high prices, is one thing; high earning power, based on skilled management or utilisation of better supplies of materials or energy, is quite another.

Earning Power and Productivity of Capital.

Bases of capitalisation.

Both are justifiable as bases for capitalisation, though the more precarious nature of the former should breed a caution reflected in the valuation of the capital; but only the latter has any economic reality behind it. Capitalisation upon the former basis not merely implies no economic service in wealth-production corresponding to the expected "earnings" derived from

holding up prices of goods, it performs an economic disservice. For by taking from investors, chiefly for the benefit of vendors or promoters, a larger amount of money than the industrial services of the business on a free competition basis would have warranted, the fresh stream of capital available for other productive purposes is proportionately diminished. This means a waste of capital resources and of total productive power from the standpoint of the industrial system as a whole.

Effect of over-capitalisation.

The truth that every sound investment causes a corresponding amount of concrete capital to come into existence and to produce actual goods and services, for the sale of which interest and dividends are paid, is of course only strictly applicable to the original act of taking up new bonds or shares just issued.* An investment which consists in buying bonds or shares from another holder of course implies no such result. It simply means the transfer of the ownership of so much industrial power from one person to another, in return for a payment which may be applied to create more economic capital or not, according to the will of the recipient. If I invested £1,000 in C.P.R. debentures when the road was first constructed, my investment meant the laying

When investment produces concrete capital.

* There is, however, sometimes no such real or concrete capital corresponding to the shares issued on the construction of a company. In American Railroads, in most instances the original real capital was raised by bonds, the shares being given as bonuses. But in most cases where the business succeeded savings have been effected out of gross income and applied to development so as to give substance to the shares, which may thus for the first time be said to have real capital behind them.

down of so many steel rails or the building of an engine. If I now invest £1,000 in buying debentures, my purchase has no such direct economic effect. It merely conveys the ownership of a part of the plant, etc., of the Railroad from another person to myself. The inconsiderable effect of my purchase upon the "market" for C.P.R. shares may be ignored. The seller of the shares may do one of three things with the money I pay him. He may spend it, instead of me, in demanding commodities for his consumption. In this case there has been no saving, or increased investment, from the social standpoint. I have made an investment; another person has unmade one. Or he may invest the money I have paid him in buying other securities from some other person who wants to "realise" on them. Here he hands over to this third person the power to spend on consumables which I have handed to him. If this third party uses it, no new capital has come into existence, merely a shift in ownership of former capital. Only in the case where the person who sells me C.P.R. debentures applies the price to take up shares in some new company does any direct industrial significance attach to the proceedings.

When investment does not produce concrete capital.

But though market dealings in established securities do not appear to affect directly the amount or situation or productivity of concrete capital, the indirect effects of such dealings upon the economic system are considerable. Wherever a market exists, there grow up more or less recog-

Effect of dealings in established securities on the economic system.

nised interests which benefit by exaggerating the fluctuations of prices. The prices of securities are particularly open to organised booms and depressions, partly by reason of the great gains which attend the successful practice of such manipulation, partly because of the essentially sensitive and incalculable nature of values affected by so many present and future factors of uncertain magnitude. A price movement once set going acquires exaggerated force from the fears and hopes of an ignorant and even a superstitious public. This occurs even with regard to purchases of actual shares for investment. Much more does it occur with regard to the buying and selling of shares, which may or may not exist, for gambling purposes. Though some forms of speculative buying and selling, practised by skilled business men, as in certain produce markets, indubitably exercise a steadying influence upon the prices of actual commodities, this is not the effect of the "gambles" of a heterogeneous crowd of plungers in stocks and shares. The bulling and bearing, though not primarily designed to influence prices of investments, does incidentally reflect itself in exaggerated movements of such values. The instability thus given to certain investments, selected for gambling uses, involves an injury to whole classes of securities, disturbing the natural distribution of the flow of fresh capital and confusing the public mind by misrepresenting the true economic value of the investment. The just and wholesome tendency for all quotations of

Causes of price fluctuations in securities.

Disturbing elements of Stock Exchange speculation.

stock to gravitate to the basis of normal earning capacity is injuriously deflected by these gambling operations, which often retain fictitious values for dead or moribund shares that are found to be convenient counters in the game. Apart from the falsification of economic facts thus brought about, it must not be forgotten that the inability of a large section of the public to distinguish clearly between investment and gambling is a means by which a great deal of "savings," which might have fructified in additions to the real capital of the world, is taken as profits by those who keep and operate the gambling shops.

Unwary public prey for the stock gambler.

So far, however, as fluctuations in prices of securities are genuine reflections of the earning power of the capital they represent, they serve a useful purpose in directing and distributing the flow of fresh productive capital. A real rise in American rails or Transvaal mines draws more new capital alike into the development of existing businesses and into the formation of new companies likely to share the actual productivity of capital indicated by the rise of prices. Similarly, a fall of prices in any class of securities furnishes a serviceable check to the application of fresh capital in that quarter. It is, therefore, of the utmost importance that trustworthy avenues of information as to real earning capacities should be maintained, and that the investing public should be left as little as possible at the mercy of artful prospectus-mongers on the one hand and gambling-house keepers on the other. For both

Effect of genuine price fluctuations in securities.

processes not merely take money from the pockets of simple men to put it into those of clever men. They cause a diminution in the actual aggregate supply of new productive capital and a wasteful misdirection in that which is supplied.

Such is the outline of the relations between the art of investment and the function of actual capital in the production of wealth.

CHAPTER III

THE DISTRIBUTION OF CAPITAL THROUGH INVESTMENT.

HAVING recognised that the function of the machinery of Investment is to organise the savings of individuals, convert them into industrial or productive power, and to distribute this power in various sorts of productive work over the different districts of the industrial world, we will proceed to examine this economic process more closely. Two main issues emerge at the outset, one having reference to the initial act of investment by which savings enter and become productive power; the other to the laws of its distribution over the economic system.

Two main issues of Economic Process of Investment.

The quantity of savings effected and applied through the machinery of investment varies of course very greatly in different nations and different classes, and different classes of investment appeal with different force to different sorts of savers.

The flow of savings into the Investment market will be determined in the first instance by the amount of surplus income over and above what is economically necessary to sustain human energy

devoted to the production of wealth. In other words, in every community a certain proportion of the productive power, issuing from the application of human energy to nature, is required for the purpose of maintaining the fund of productive power intact. Any productive power not needed for this purpose can be applied to creating non-consumables, i.e., tools, developmental works, raw materials, and other forms of concrete capital designed to promote the larger or better production of wealth in the future. This surplus, beyond the expenditure in maintenance, is the theoretic maximum of saving for any nation or other group. In some conditions of society it is non-existent or negligible in amount, the niggardliness of nature, or the backwardness of the industrial arts, or the natural indolence of the inhabitants, or the insecurity of property, confining their productivity to the amount of wealth necessary to support the stagnant or slowly growing population. Moreover, where some surplus does emerge, it need not be "saved" and converted into "capital." A conventional standard of comfort may consume it in current expenditure. This standard of comfort may or may not be such as to evoke an increase of human energy available for future economic work. It may go in waste or luxury, or it may go in improving the physique and intelligence of the people. But such expenditure of the surplus, whether economically good or bad, precludes it from figuring as savings.

Definition of savings.

Distinction between surplus income and savings.

Thus then the actual fund available for saving

is the surplus over what is needed to maintain the conventional standard of comfort. Though some of this surplus in progressive communities will be expended in raising the standard of comfort by direct increase of expenditure upon consumables, all of it is available for saving and under sufficient stimuli will be saved.

What the amount of surplus income depends upon.

The amount of this fund in different countries will depend mainly upon two considerations; first, the state of the industrial arts; secondly, the distribution of income among the several classes of the community.

Until the main branches of the textile, metal, and other principal manufactures, have passed out of the stage of handicrafts, utilising division of labour, machinery, and mechanical power in a factory system, while transport has also been placed upon a modern mechanical footing, a country is not in a position to possess a large surplus for investment. Even so ingenious and industrious a people as the Chinese, unusually thrifty in their habits, can only possess a comparatively small surplus over the current needs of an abounding population. Until the 19th century there was in no part of the world either a great demand for capital or a great possibility of supply. The pace at which savings were accumulated and applied to develop the new factory system on our great coalfields in the early decades of last century was a novel phenomenon in economic history. An enormous proportion of the new wealth of Lancashire must have been put

Origin of capital supply and demand.

back into work of development. Probably the proportion diminished as the employing and the working classes alike evolved new wants and built up rising standards of consumption. For though improved intelligence and general efficiency followed a rising standard of consumption, it is likely that, while the volume of saving was continually increased, its proportion to what was spent grew less. For nearly half a century Great Britain possessed so large a start in the new industrial arts that her savings and investments were probably greater than those of all the rest of Western Europe. With these savings she was enabled, not merely to finance her own railways and mining development in the mid-century, but to spare large funds of wealth for similar enterprises in the United States, Australia, South America, and the Continent of Europe.

Savings and Investments of Great Britain in early 19th century.

Not until 1860 did even the more advanced Continental countries begin the full task of modern equipment, and Germany and France, though possessed of considerable capital by 1870, remained far behind Great Britain both in factory and railway development. The United States too only began adequately to realise its potentiality of wealth-production after the close of its civil war and the era of financial embarrassment which ensued. Though the other nations, profiting largely by the experience of Great Britain, were able to conduct their industrial transformation with great rapidity, it took them a generation to discover and apply the natural re-

Great Britain the pioneer of industrial development.

sources of mine, field, and forest which they severally possessed, to create a fully effective transport system, and to gather in and train a labour-class for the modern industrial life, building or extending cities in which this industrial and commercial population were to live and work. Even now only a comparatively small part of the temperate zone is fairly standardised for the chief mechanical industries. The degree in which the nations have adapted themselves to the new processes of production and transport is the first measure of their effective saving and investing power.

Industrial Development of the Nations.

But a mere measurement of the wealth of the several nations, as aggregates, or per head of the populations, does not indicate the true saving and investing power. Much depends upon the distribution of the national income among the several component classes. Since rich men can spare better, and so save more easily, a considerable share of their income than poorer men, it is reasonable to suppose that they do so. This will lead us to believe that a nation or community in which the income is unequally divided is likely to yield a larger quantity of saving. Though the possession of riches induces luxury and even extravagance of living, it is indisputable that the rate of saving normally rises in direct ratio to income. Generally speaking, the highest rate of saving will be found in those classes of business men who, after attaining a fairly high level of comfort, find their incomes still rising rapidly. A rich aristocracy of settled habits of luxury and

Saving propensities of rich and poor people compared.

conventional display almost certainly save less than an equally prosperous body of men belonging to the *nouveaux riches*. But, taking a broader classification, we shall generally find a higher proportion of saving to spending in nations where rent, interest, and profits absorb a large proportion of the total revenue. The existence of a millionaire class is a tolerably safe index of a high rate of potential and actual saving. This statement of the apparent advantage of inequality of incomes requires, however, this important qualification. If the inequality is such as to maintain a large labouring population, ill-nurtured, ill-educated, and deprived of adequate incentives to acquire improved industrial efficiency, though immediately favouring a high proportion of saving, it will, by retarding the general pace of industrial progress, reduce the rate of further growth of income, and so limit the future aggregate amount of saving.

How the progress of saving may be retarded.

Varying degrees of saving ability.

These mainly objective conditions, relating to the size of the surplus income available for investment, are not, however, reliable indices of actual saving apart from consideration of the characters of the various nations, classes, and even individuals. The economic surplus can be saved and invested, but, how much of it will depends upon the degree of foresight, regard for the future, and power of self-restraint possessed by the owners of such surplus. A Scot or a Jew with a given income will usually save more than an Englishman, a French peasant more than a Parisian, a Chinaman more than an Irishman. Inherited

character and traditions, imagination and ambition, some definite appeal to acquisitiveness, an immense variety of characteristics and conditions, go to determine the actual rate of saving in a nation or a class. Other things equal, the men who most vividly and constantly realise the future for themselves and their families, will actualise the largest proportion of their potential savings. But not even a man of provident mind will save and invest capital, unless he has confidence that he will be able to realise it, if he wants, and to obtain such reward in the shape of interest as to make it worth his while to postpone some present enjoyment. In other words, he must have at his disposal a choice of investments of which he can have some knowledge, and in which he entertains confidence. Every increase in the area of reliable investment for any class of men thus exercises a stimulative influence on saving. This confidence is partly a subjective, partly an objective condition. It means that the art of investment must be sufficiently developed to bring enough opportunities for placing their savings within the reach of the saving classes, and that the latter have sufficient intelligence and faith to recognise the value of these opportunities. An ignorant farmer may, and often does, keep his savings in a stocking, though there may be close at hand remunerative and safe uses for them.

How the rate of saving is determined.

Reliable investment a stimulus to saving.

Every extension of the effective area of investment thus effected through improved education and reliable advertising, by enlarging the choice

of investments for a saving class, not merely will evoke more saving, but will distribute it more efficaciously.

Three important technical conditions are, however, essential to secure a proper utilisation of saving power in a community. First comes the efficiency of local banking and investing arrangements. The power to save and the will to save are comparatively ineffective without the existence of local instruments for the conduction of this economic energy. It is falsely said that capital is timid. History shows capital to be extremely venturesome. But certain orders of small capitalists are very timid. They were afraid to let their savings out of their sight, they would only invest in some business undertaking close at hand, or in real estate in their immediate neighbourhood. To turn these innumerable little rills of saving into the broad river of national or international investment is a slow and difficult task. But in England and in other advanced countries enormous strides have been made in this process of conduction. The extension of branch banking and insurance, reaching large sections of the lower, middle and upper wage-earning classes. is an economic innovation of the first importance. For the lowest grades of income-tax payers and the highest grades of wage earners have been growing at a very rapid rate in this country, yielding a large new supply of capital which required great trouble to collect. So far as banking is concerned, the extension of branch banks,

Timidity of certain small capitalists.

Banking and insurance as capital conductors.

proceeding *pari passu* with a rapid process of amalgamation,* not only has improved the technical apparatus of local finance, but has increased the actual security of saving. The small farmer or struggling shopkeeper is no longer haunted by a dread lest the bank which has got his hard-earned savings should stop payment. The habit of insurance for both life and property is similarly spreading by the growth of an elaborate network of capitalistic and co-operative agencies. Though the working expenses of many of these consume an enormous proportion of the premiums, while lapses of policy upon the one hand, reckless or dishonest administration on the other, greatly hamper the efficiency of this branch of saving, they play a considerable part in gathering in surplus for investment. Though, in many rural communities, local credit is best utilised for purely local purposes, and an apparatus of Land and People's Banks is developed to carry on the work, especially in the farming industry, such savings as are not required for these narrower purposes of mutual aid are made available in an increasing measure for wider outlets of investment by an ever-closer communication between local and national finance.

Increased security of saving.

Insurance as a branch of saving.

Hardly less significant is the extension of agencies for dealing in stocks and shares. By the

* "At the end of 1878, the number of joint-stock and private banks, excluding the foreign and colonial banks, was 336, with 1,789 branches. At the end of 1908 the number of banks had been reduced to 84, while the number of branches had increased to 5,072."—Mr. F. H. Jackson, Presidential address to the Institute of Bankers, Nov. 10, 1909.

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establishment of Stock Exchanges in large provincial cities, the establishment of professional stock brokering businesses in all considerable towns, the use of the post and the press and the tape, for bringing scattered investors into touch with the wider markets, the saving and speculating energy of the nation has been stimulated and directed into the wider streams of finance.

Important influence of stock and share operations on saving.

Though much waste and not a little dishonesty inhere in the working of this system, it must be regarded upon the whole as performing a valuable function in expanding the area of investment and the ultimate productivity of large quantities of savings, which would otherwise not have been made at all, or would have stagnated in some comparatively barren local employment. As this apparatus of banking, insurance, and stock operations, spreads over the whole area of the civilised world, and the public confidence in its efficiency and honesty is established among all the strata of the saving population, the flow of new capital available for cosmopolitan work will become ever greater.

Banking, Insurance, and Stock operations increase the flow of capital.

The security of such an apparatus is not, however, merely a matter of economic equipment and business enterprise. It hinges in two ways upon the art of Government. In order thus to do the work of the world a man and his money must be widely parted. It becomes more and more difficult for him to follow his bit of savings in its career through the hidden channels of investment. Hence an increasing need of legal regu-

lation and protection. The law must secure to him certain rights of information in regard to companies which offer him shares, and some representative control over the property of which he is part-owner; it must guard him against certain forms of fraud or mal-administration which he cannot personally check, by requiring some publicity of accounts and sound methods of bookkeeping. The forms and the efficacy of such legal protection vary very widely in different countries. Where either the Company laws or their administration is defective, there is a corresponding weakness in the efficiency of investment. Financial cunning cannot operate unchecked upon credulity without damaging reactions upon thrift. Stringent legislation and administration in regard to issue of money and of credit, flotation and working of insurance and finance companies, and to dealings in shares, are to be considered as protective not merely of the saving or investing individuals, but of the financial and industrial system. The real damage done by recent revelations in the insurance and banking institutions of the United States consists in a weakening of the subjective roots of credit, checking and retarding the free flow of savings, or limiting the area of investments.

Legislative protection for the investor.

Detrimental effects of financial malpractice.

The other political factor relates to the degree of stability and enlightenment possessed by or imputed to the Governments of the various states. For the bad government of its country every business enterprise, public or private, which seeks

the money of investors, pays a heavy price. The rate at which a government can borrow is a formal register of its character as displayed in its history. A foolish or criminal war, leaving a mountain of indebtedness, or the rankling animosity of some powerful neighbour, internal dissensions threatening the public order, the reputation of public extravagance or maladministration, the memory of past acts of repudiation, a failure to develop the intellectual or material resources of the nation in accordance with the principles of modern enlightenment—all such grave defects are reflected in national credit. Bad public credit in its turn again reacts upon the credit of private companies, thus retarding the actual industrial and commercial development of whole areas of the world's surface.

Government maladministration and national credit.

The term in which these various governmental influences are gathered for common expression is *Security of Property*. In order that fresh capital, drawn from the widest area, may flow most freely into the most productive channels, there must be, first, Freedom of Investment; secondly, Security of Ownership; thirdly, Security of an adequate return from the yield of capital. The various ways in which government by legal, administrative, and financial measures may assist or injure these facilities cannot profitably be discussed in detail here. It must suffice to name the chief of them.

Three essentials to free-flowing Capital.

Laws affecting the ownership, tenure, and disposition of land, may limit in various ways liberty

How Government Measures affect liberty of Investment.

of investment. Restrictions upon the ownership or leasing of land by foreigners, or upon the quantity of land owned or occupied by a company, or upon the utilisation of water or other powers, laws of inheritance or transfer, or customs endowed with legal validity, may interfere in various ways with investment in mining, agricultural, and transport companies. The duration and degree of protection accorded to investors and patent-holders, and the conditions under which franchises are given out by public bodies for the working of state or municipal monopolies, are often of prime importance in determining large classes of investment. There can be no doubt, for instance, that the development of electric lighting and electric traction in Great Britain was impeded by legal conditions unduly curtailing the prospect of profits from successful operations.

Company Law and freedom of Investment.

The effect of protective tariffs, bounties, or other subsidies, on certain mining, manufacturing, or other industries, will inevitably serve to draw into these channels of investment a larger quantity of free capital than considerations of productive utility would warrant. The state of Company Law in a country must, of course, be fraught with important direct influences upon freedom of investment, according to the liabilities it imposes upon, and the rights and protection it secures for, investors and other creditors. Last, not least, the taxing system of each country is liable to impose various burdens and restric-

tions affecting the conduct of a business and the net yield of the capital engaged in it. In not a few countries special taxes are placed upon the profits of corporate enterprise, sometimes progressing with the aggregate amount of profits, a direct interference with the tendency of capital to group itself in the most productive forms. All duties upon transfer of shares, beyond a low necessary registration fee, operate similarly as interferences with the fluidity of investments. Where, as in Great Britain, compulsory returns of income and collection of the tax at the sources enforce the operation of the tax more rigorously in the case of companies than in that of private businesses, this difference of rigour also acts as a discrimination against this type of business structure.

Investment and the Burden of Taxation.

Finally, the attitude of the public mind towards the administration of justice in regard to the property of public bodies or of companies is by no means a matter of indifference. The working of the jury system in this and other countries usually betrays a bias against corporate property where one of the litigants is a private citizen, though this bias may often be more than offset by the advantages which the larger financial resources of the public body or the company can muster for the more expensive processes of litigation. In a highly developed commercial community both legislation and administration will be better adapted to secure corporate forms of property.

Public opinion and Corporate Property.

In considering the relative advantages of various countries (1) in regard to investing capacity of the inhabitants (2) as areas of investment, we must take into due account all the foregoing factors, many of them not operating independently but in close relation to one another.

CHAPTER IV

THE DEVELOPMENT OF FOREIGN INVESTMENTS.

BEFORE proceeding to examine (1) the geographical distribution of the ownership of invested capital, or negotiable securities, and (2) the geographical distribution of the business operations in which this capital engages, it may be well to set out the principal economic factors which operate in different departments of industry to bring businesses more largely within the sphere of joint-stock enterprise.

Economic factors leading to Joint-Stock Enterprise.

In every trade, though businesses of various sizes may be found, there will be an advantage in favour of some sizes as compared with others. While there will be certain sorts of farming, shopkeeping, or manufacture, in which little businesses worked on small capitals may hold their own, or work more profitably than bigger businesses, in most industries businesses of comparatively large size have the advantage. Wherever expensive machinery or other plant is essential, where large credit is needed to deal

with fluctuating trade and prices, where success depends largely upon advertising and the acquisition of large markets, where elaborate division of labour is involved, no business conducted with small capital can survive. Now while a rich man, or his family, may be able to finance a fairly large manufacturing or trading business with their own resources, or by private borrowing, many modern manufacturing and trading businesses exceed the limits of such private individual enterprise, demanding a co-operative finance.

Businesses requiring co-operative finance.

Though the size of an effective single plant, a textile factory, an ironworks, a retail store, may not exceed the means of a single owner, the business economies of operating a number of such factories, works, or stores, as a single enterprise, will drive an increasing proportion of such businesses into joint-stock companies. The economies of machinery and of fluid credit are the chief determinants.

Increasing importance of Finance and Transport.

But while manufacture and commerce are the two most obvious and ancient branches of industry, modern conditions tend to give an ever growing importance to other economic activities, in particular to transport and finance. Everywhere transport in its larger signification, including the apparatus for the carriage of persons, goods, and information by land and sea, and finance, including all departments of banking, insurance, and investment work, occupy a position of increasing size and influence in the economic world. The proportion of capital and labour

engaged in these enterprises continually grows, and the magnitude of the separate businesses is such as to bring them almost entirely within the field of joint-stock investment. Every railway or steamship business, every modern bank or insurance business, requires co-operative capital.

Growing demand for co-operative capital.

Modern mining operations, mainly engaged in supplying the coal and iron which are material and power for the machine economy in transport and manufacture, also necessarily absorb an increasing share of capital, all of which must be supplied by modern processes of investment. The working of the new industrial system involves the aggregation of large masses of industrialists and commercialists in great cities, and the development of modern city life has rapidly evolved new industries for the production and supply of various civic services, the water, lighting, traction, and other great capitalistic works which have in large measure passed under public management and control. But whether left to private enterprise or taken over by municipalities, such businesses furnish new enormous areas of investment for private savings.

Reasons for increasing need of co-operative capital.

The apparatus for the supply of many of those non-material wants that belong to our civilisation, the information, recreation, education, cultural, and professional services, is largely capitalistic and affords new areas of investment. Newspapers, publishing firms, and a large part of the theatrical and musical supply have passed under this form of capitalism.

Wider area of appeal for investment.

These different fields of modern joint-stock capitalism, of course, vary widely in the degree of freedom of investment that they offer. Regarded as negotiable securities they differ greatly in the area of their market. Some are freely international, others national, others narrowly local in their ownership and market. But the modern tendency is not merely to increase the number of joint-stock businesses, but to increase the area of appeal, so as to bring on to the national, or even the international, market shares which were formerly of purely local interest. A main object of Investment Companies is to achieve this more discriminative placement of capital. Since the various countries of the world are very unequally developed, both in capacity for saving and investment and in capacity for profitable utilisation of capital, it is evident that the main currents of the flow of new capital will be determined by these differences. The investing power will be greatest in the older and more developed countries, the capacity for profitable utilisation greatest in the newer and less developed countries, provided that these latter have attained a sufficient status of political security. When the capitalistic development of a country has reached the point which yields a saveable surplus, in excess of the amount required to meet further pressing demands at home, that surplus will spread itself in foreign investments, forming a portion of the fund of world capital, the economic purpose of which is to standardise the world for

Investing Power and profitable utilisation of Capital.

capitalistic production. So far as purely economic forces have free play, capital tends to distribute itself in proportion to the developmental needs of the various countries. This of course by no means implies a tendency to place all countries on an equal level of agriculture, manufacture, or commerce. Free capital will have regard to the abundance and kind of natural resources in each country, the needs and capabilities of its population, and the home and foreign markets which can be profitably supplied.

Capital distribution regulated by need for development of country.

The work will proceed along the lines of assimilation and of specialisation simultaneously. A vast proportion of the free capital hitherto available for world-use has been applied to the standardisation of national communications, by railroads, shipping, and telegraphic services, docks, harbours, etc. This work of road-making, the object of which is to make all parts of the world accessible, is of a fairly uniform and routine character: it constitutes the first line of development. The second line consists in the discovery and exploitation of any special mining, agricultural, or other natural resources available for the world market. Gold or other precious metals, oil, rubber, ivory, are in the first rank of such commodities; tea, sugar, tobacco, iron, coal, timber are usually later claimants on world-capital. Here we enter the more specific development of material resources. As the free flow of world-capital advances in this primary work of road-making and exploitation of natural resources, the

Lines of development in which capital is utilised.

demands of modern city life begin to press their claims, and capital flows in to speculation in sites, erection of business and residential blocks, hotels, theatres, street cars, and all the elaborate material equipment of the twentieth-century city, substantially the same in Mexico, Japan, or Madagascar as in England or Germany.

Nearly all the world-capital is absorbed in this fundamental work of material equipment, and in evoking certain specially valuable materials for world markets. Comparatively little goes directly into ordinary manufacturing and commercial businesses for the supply of the needs of the inhabitants of the foreign land. But indirectly considerable amounts of invested capital soon begin to find smaller channels of lucrative, or speculative, employment in stimulating the home industries, and in raising manufactures on the foundations of mining and agriculture. Though foreign investors are long shy of industrials, they are soon induced to put money into general investment companies under the names of banks, insurance, land, or other financial corporations. The main use of these financial middlemen is in the nicer detailed distribution of world-capital for local development of industrial resources. Comparatively little foreign capital is directly invested in manufacturing enterprises. Of these breweries and distilleries form the most important class.

Little capital directly absorbed by commercial undertakings.

Banks and Financial Corporations the distributors of Capital.

As a backward country begins to fructify under the stimulus of a flow of capital from outside, its growing wealth is not all taken out in divi-

dends to foreigners. Much remains in the country, owned or administered by the more enterprising local business men. As time goes on and development proceeds apace, the hold of the creditor-countries usually becomes weaker. This is sometimes denied. It is contended on the contrary that a debtor-nation tends to get deeper and deeper into debt, losing continually a larger share of the ownership of any valuable assets which it may possess. And no doubt there are cases which appear to conform to this interpretation. A government, like an individual, may become a spendthrift, using what credit it possesses to plunge into extravagant and unproductive expenditure, and borrowing more money to pay the interest on the earlier loans. The Russian and to some extent the Australian governments are obnoxious to this charge. But, however wasteful and excessive such borrowing may be, the strangling process is not so inevitable as it seems. Even the interest upon the huge loans which the Russian government has effected in recent years is probably a very small percentage upon the growth of real wealth in the country, and does not really mean that the resources of Russia are passing more and more into the possession of foreign bondholders. Still less is this true of Australia, where a far larger proportion of the borrowing is represented in railways, harbours and other tangible productive assets. But even were it the case that, at certain epochs in the development of a backward country,

Position of the debtor-nation.

Russian and Australian Government Loans.

borrowing proceeded so rapidly that foreign was growing faster than domestic ownership, such periods must be treated as exceptional. Where, as is usual, borrowed capital is mainly applied to genuine purposes of development, its fructification will be so great as to do far more than furnish the bare dividends upon the loans, and this excess will remain in the possession of the propertied and business classes of the country, forming a fund of home-made capital which later on will largely be utilised in paying off the foreign obligations. The later growth of manufacturing and commercial businesses will be conducted by home-made capital, and, though large holdings of shares in railroads and other developmental work may remain in foreign hands, there will be a constant tendency to displace this alien ownership by home investors. The United States, the largest field for foreign capital a generation ago, exhibits this tendency to revert to national ownership in the most marked degree. But, as we shall see later, it must be recognised as a natural economic, not as a merely political or patriotic tendency.

Borrowed Capital applied to development purposes.

Tendency of foreign-held Capital to revert to national ownership.

. . . .

This brief summary of the main obvious economic factors influencing the flow of invested capital may serve as introduction to and commentary on the following attempt to present some statistical estimate of the part played by the chief countries as investors and as recipients of loanable capital.

The most comprehensive estimate of the relative advance of the principal countries of the world in the art of financial investment is presented by Mr. Charles A. Conant, in "The Atlantic Monthly," for January, 1908. Working upon a Table prepared by the French economist, Alfred Neymarck, he reaches the following results for the European countries in 1900, alongside of which he places an estimate for the United States and Japan in 1905.

Advance of Financial Investment in chief Countries of the world.

The values stated (in dollars) will of course include investments abroad as well as at home owned by inhabitants of the several nations.

Estimated Outstanding Securities in Europe and the United States, 1900:—

Comparative table of Investments of various Countries.

Country.	Par value of Securities owned.	Population.	Amount per capital.
	$		$
Great Britain....	26,400,000,000	42,789,600	616·97
France..........	19,500,000,000	38,961,950	500 94
Germany........	10,000,000,000	56,367,180	177·41
Russia..........	5,400,000,000	129,004,270	41·86
Austria-Hungary	4,400,000 000	45,405,270	96·90
Netherlands	2,200,000,000	5,431,000	405·08
Italy	2,300,000,000	33,218,330	69·24
Belgium	1,400,000,000	6,985,220	200·42
Spain	1 300,000.000	18,618,090	69·82
Switzerland	1,100,000,000	3,315,450	331·78
Denmark........	600 000,000	2,646,770	226·69
Sweden and others	400,000,000	51,537,010	7·76
Europe	75,000,000,000	434,280,140	172·70
United States, 1905	35,514,351 382	83,260,000	414·54
Japan, 1905	1,563,412,951	47,975,110	29·70
Aggregate .... $	112,077.764,333	565,515,250	196·17

Supposing this estimate to be even approximately correct, it indicates Great Britain, France, the United States, and Holland as the countries which have made the farthest advance in the art of investment, if, as is reasonable, we take as our best index the amount per capita of invested capital. It will, however, certainly be found that since 1900 Germany has made both an absolute and a relative advance. The German estimate for 1900 is evidently little better than a guess, and it is probably much below the mark.

Countries showing greatest amount of Invested capital per capita.

It would be extremely interesting to know what proportion of the aggregate wealth of each country has passed into the form of negotiable securities. Mr. Conant, speculating on this question, expresses the view that "about 45 per cent of the wealth of Great Britain is in the form of securities, about 40 per cent of the wealth of France, and only about 25 per cent of the wealth of Germany." The ratio for the United States he puts at about 23 per cent. But this speculation is of very dubious worth, being apparently based upon a computation of the total wealth of European countries made in 1896 by Mr. Michael G. Mulhall for the United States Census. Mr. Mulhall's estimate for Great Britain, of eleven and a half milliards, is probably a good deal below the mark. Sir Robert Giffen at any rate in 1900 placed the figure considerably higher, holding that "the whole capital of the nation at the present time is probably not far short of £15,000,000,000 sterling, while the

Estimated proportion of Aggregate Wealth represented by Securities.

annual increase must be at least between £200,000,000 and £300,000,000 sterling.*

Neither in regard to the proportion of the total wealth of a country capitalised in securities, nor in regard to the proportion of such securities owned inside the country, is sure information anywhere available. Difficulties of valuation, especially in relation to three classes of assets, viz., (a) public wealth of a non-marketable order, (b) capital in the shape of private businesses, and (c) property belonging to the working-classes, impart a most precarious character to the first computation, while the continual sale of securities, often to foreigners, makes it impossible to state with any accuracy how much of a negotiable stock is at any given time owned within the country. Finally, the records of investment render possible a good deal of duplication. Where investment companies or banks hold capital in the securities of other companies, there is some risk of the same properties counting twice in a general attempt to assess the value of all securities. Moreover where securities are quoted on the Exchanges of several countries, an attempt to assess the value of national investments by reference to such accounts is evidently illusory.

Computation of wealth represented by Securities unreliable.

Why the exact amount of Wealth realised in Securities is unobtainable.

But while exact statistics are not available, there is plenty of evidence to indicate the rapid pace at which negotiable capital is growing in most advanced countries.

* "Economic Inquiries," vol. 2, p. 288.

The following Table compiled from official returns shows the constant rapid growth of the number of registered Joint-Stock Companies in Great Britain, and the increase of paid-up Capital which they represent:—

Table of Statistics of Joint-Stock Companies.

	Total No. of New Companies.	Total Nominal share capital of new Companies	Total No. of Companies.	Total paid up capital of Companies.
		£		£
1892	2,607	103,403,331	16,173	969,283,634
1893	2,617	96,654,161	17,555	1,013,119,359
1894	2,970	118,431,570	18,361	1,035,029,835
1895	3,892	231,368,077	19,430	1,062,733,821
1896	4,735	309,523,047	21,223	1,145,402,903
1897	5,229	291,117,559	23,728	1,285,042,021
1898	5,182	272,287,690	25,267	1,383,593,162
1899	4,975	245,939,676	27,969	1,512,098,098
1900	4,966	221,827,934	29,730	1,622,641,406
1901	3,433	144,760,333	31,429	1,725,940,512
1902	3,929	156,983,861	33,259	1,805,141,165
1903	4,075	126,606,015	35,965	1,849,455,005
1904	3,831	92,526,113	37,287	1,899,648,675
1905	4,358	117,179,333	39,616	1,954,337,135
1906	4,840	136,738,249	40,995	2,003,392,061
1907	5,265	137,907,836	43,038	2,061,010,506
1908	5,024	104,441,189	45,304	2,123,492,957
1909		141,630,296	46,474	2,163,132,789

The paid-up capital in Joint-Stock Companies is thus seen to have much more than doubled in the course of seventeen years.

Growth in paid-up Capital of British Railways.

During the same period the paid-up capital of British Railways, not included in the above table, increased from £944,357,000 in 1892 to £1,314,406,000 in 1909. Though the capital of Municipal Tramways and of certain Joint-Stock

Banks is not included in the above Table, it may be taken as the best index of the advance of negotiable securities in this country. The advance in sixteen years is far greater than that of the national income as attested by Income Tax returns, or than the growth of property assessed for Death Duties. It is unlikely that the total aggregate of national wealth has increased by 30 per cent. during this period in which company capital has more than doubled itself.

Advance in paid-up Capital compared with National Income.

CHAPTER V

THE DISTRIBUTION OF FOREIGN INVESTMENTS.

WE have seen reason to expect that the nations which have advanced furthest in financial capitalism will have the largest surplus available for investment outside their own country. Great Britain, France, Germany, Holland are known to be great creditor nations, owning a much larger quantity of capital in other lands than the inhabitants of these or any other foreign countries own of theirs.

Present and future position of United States in Finance.

Among the newer countries the United States alone is to be placed in the front rank of finance. As such her position is noteworthy. Though signs now indicate that her demand for further capital to develop her great internal resources is slowing down, and that foreign investments will begin to tempt an increasing flow of her new capital abroad, home needs have hitherto absorbed the vast majority of her savings. Though in the

last two decades she has bought back large quantities of her huge debt to foreigners incurred in the two previous generations, especially in the way of railroad finance, and has invested largely in South American securities, she doubtless remains to no inconsiderable extent a debtor to European, and particularly British, investors.

Amount of British Capital invested abroad.

Great Britain, however, is by far the largest foreign investor. She began the process earlier, has extended her investments more widely, and reaps a far greater return in dividends than any other nation. It will be of interest to examine the size and the distribution, geographical and economic, of these foreign investments. Mr. Paish of the "Statist," in an important paper read in January, 1911, to the Statistical Society, estimated the aggregate of our capital invested abroad at about £3,192,000,000, imputing to it an income of nearly £160,000,000.

British Capital invested abroad through mercantile and banking houses.

This sum does not, however, include capital invested in our mercantile marine, an investment which may be regarded as half-foreign in its employment. Nor is any allowance made for the capital privately placed abroad through mercantile and banking houses. A proper allowance for British capital thus privately invested in companies abroad, estimated at not less than £300,000,000, together with a further allowance of from 250 to 500 millions for shipping, would

raise the aggregate of our investments abroad to a figure not far short of £3,500,000,000.

Total amount of Great Britain's invested Capital in 1900.

If this figure be provisionally accepted, and Mr. Conant's estimate of the total invested capital for Great Britain in 1900 be raised from £5,300,000,000 to £6,000,000,000 to allow for recent additions, it will appear that somewhat more than half of our invested capital is placed abroad.

Foreign investments of France and Germany.

Our general survey of the economic forces directing investment will have led us to expect that Great Britain, having begun earlier and advanced further in the development of her own capitalistic structure, should place a larger amount of her more recent capital abroad than other nations whose capitalistic career began later and whose savings therefrom would still for the most part be absorbed in home undertakings. Bearing these considerations in mind it is not surprising to learn that British foreign investments probably exceed those of all other European countries taken together. The aggregate for France was estimated by M. Neymarck as 31,200,000,000 francs, or about £1,250,000,000 in 1900. This sum may, perhaps, be raised to £1,500,000,000 for comparison with our later British estimate. Germany's foreign investments were estimated by Paul Deyn in 1902 at a little over £900,000,000. An elaborate investigation of the German Admiralty Office,* however, gave the somewhat

* Die Entwicklung der deutschen See-interessen in letzten Jahrzehnt., p. 179.

lower figure of sixteen milliards of Marks or £800,000,000 for 1904. If this be taken as the most authoritative estimate, the most ample allowance for recent years will not bring it up to £1,000,000,000, especially when we consider that during the last decade there is good evidence to show that the requirements for home development have been absorbing an increasing proportion of Germany's new capital.

Belgium's new capital surplus.

Belgium is probably the only other European country whose capitalistic position gives her a large surplus of new capital beyond the current domestic needs, and that sum, though considerable for a small country, will not bulk largely in comparison with that of France or Germany.

Increase in Great Britain's foreign investment of new Capital.

Though complete statistics of our foreign investments are not procurable, and even the careful estimates of Mr. Paish admit a considerable margin for error,* it seems certain that the tendency of recent years has been for foreign and colonial securities to absorb a rapidly increasing proportion of our new capital.

The tabulation of British Investments during

* It is not possible to know how many of the shares taken up in new companies brought out in London are bought for foreigners, or how many are subsequently acquired by foreigners. Moreover, the examination of companies which forms the basis of Mr. Paish's computation of invested capital does not appear to take account of dead capital put into companies which have failed and disappeared. Yet such capital was actually provided by our saving and investing public, though it may have acquired no earning capacity.

the last ten years* present in an exaggerated form the actual tendency.

Percentages of Home, Foreign, and Colonial investment of British Capital.

INVESTMENTS PERCENTAGES.

		English.	Colonial.	Foreign.
1899	...	53 %	22 %	25 .
1900	...	80	14	6
1901	...	75	18	7
1902	...	56	26	18
1903	...	39	47	14
1904	...	40	29	31
1905	...	31	29	40
1906	...	30	22	48
1907	...	25	22	53
1908	...	26	32	42
1909	(to Sept.)	10	34	56

The opening years of this period marked an epoch of immense activity and expansion in domestic enterprises, reaching the high water mark in 1900, when four-fifths of the new capital was absorbed at home. But though a table starting from this quite abnormal position over-accentuates the actual tendency, there can be no doubt that the diffusive forces spreading our new capital over wider fields of investment are steadily gathering force.

Widening area of British investments.

This truth is, perhaps, more solidly attested by the official records of income derived from British investments in colonial and foreign Government and railway securities, which furnish the nucleus of our estimates for total income from foreign investments.

* "Bankers Magazine," vol. lxxxviii., p. 616.

"Income from Indian, colonial and foreign Government bonds and stocks, municipal stocks and railway securities."

Annual Income from British Investments in foreign and colonial Government and railway securities

	Total.
	£
1886-7	44,508,002
1887-8	46,978,371
1888-9	49,999,808
1889-90	52,310,212
1890-1	55,488,832
1891-2	54,728,770
1892-3	55,170,502
1893-4	55,118,029
1894-5	53,506,258
1895-6	54,901,079
1896-7	56,318,967
1897-8	56,639,666
1898-9	59,709,903
1899-1900	60,266,886
1900-1	60,331,525
1901-2	62,559,479
1902-3	63,828,715
1903-4	65,865,306
1904-5	66,062,109
1905-6	73,899,265
1906-7	79,560,116

Percentage of increased Income over twenty years.

These figures indicate upon their face an increase of income from this class of investments amounting to more than 90 per cent within twenty years. The increase, moreover, is seen to be far greater in the latter of the two decades. Though this, of course, cannot be taken as an exact, or even approximate, measure of the rate

of new investments, since a larger proportion of such capital must take several years before it will ripen in current income, it certainly does furnish strong support to the hypothesis that an increasing proportion of our new capital goes abroad. Though a period of brisk expanding trade at home will retard the growth of this tendency, there can be no question about its normal operation.

When foreign Investment of British Capital becomes necessary.

When the safest, most fundamental, and, upon the whole, most profitable employments for capital at home have already been amply furnished by our saving and investing classes, it is natural, desirable, and even necessary, that larger quantities of this fresh capital should be placed further afield, applied in other countries to the same sorts of productive enterprise which in former times absorbed all the new capital for home use. An examination of the uses to which our capital that flows abroad is put shows that it is in fact applied mainly to such purposes.

Classification of British Investments in foreign and colonial securities.

A condensed classification of our foreign and colonial investments, as apportioned by Mr. Paish (in an earlier paper, June, 1909) to their several occupations, yields the following results :—

Government Loans and Municipal Stocks	757,460,000
Railways	1,198,991,000
Banks and Finance Companies	241,128,000
Breweries and Distilleries ...	17,205,000
Canals and Docks	5,974,000
Electric Light and Power ...	7,686,000

Gas	16,419,000
Mines	243,386,000
Nitrate	10,903,000
Oil	14,268,000
Rubber	5,433,000
Tea and Coffee	21,399,000
Telegraphs and Telephones ...	34,235,000
Tramways	35,289,000
Waterworks	6,352,000
Commercial, Industrial, etc. ...	77,610,000
	£2,693,738,000

Total amount of British Investments in foreign and colonial Securities during sixty years.

These figures show that up to the present the overwhelming majority of the investments are in what may be termed developmental work. The second item in this account, railways, is seen to absorb nearly one-half the total sum. If, indeed, we add to this the capital invested through the government and finance companies in railways and roads, and the amount devoted to tramways, telegraphs, and telephones, we recognise that more than half our capital has gone to opening up and improving communications with the rest of the world, in a word to road-making. Of the remainder, a very large share has gone to developmental work of the next order, to canals and docks, waterworks, lighting and other public services, and to the various mining operations. The third line of development, that of the exploitation of organic materials, by the cultivation of the soil, has not directly taken any large share

British capital invested abroad: its application.

of our capital, though recent speculation shows that our finance is ripening for this order of investment. As yet, only a small percentage of the whole is employed either directly or indirectly in manufactures or commerce, breweries and distilleries forming the only class sufficiently important to deserve separate recognition.

British Capital invested abroad: three years' figures.

The statistics above quoted cover the estimated aggregate of all our investments in the last sixty years. It might be supposed that recent times had materially changed the economic character of the new investments. But an analysis for the three years ending July, 1909, gives no support to this conjecture.

	1908-09.	1907-08.	1906-07.
	£	£	£
Government Loans	64,840,459	27,620,206	17,979,150
Municipal Loans	13,801,404	9,105,115	2,559,123
Railways	52,783,929	51,552,561	34,549,245
Other	44,240,375	21,866,578	34,234,383
Total	175,666,167	110,144,460	89,321,901

Predominance of Public Loans and Railways.

Public loans and railways still maintain their predominant place as claimants for new capital, and closer analysis of the miscellaneous group shows that municipal plant and mines continue to take a large proportion of the remainder.

Great Britain's capital investments * in other lands since 1st July, 1906 :—

* Amount calculated at the price of issue, and exclusive of loans raised to repay former loans.

	1908-09. †	1907-08.	1906-07.
	£	£	£
Government Loans—			
Indian	7,275,000	4,950,000	3,525,000
Colonial	27,072,615	12,031,269	9,593,383
Foreign	30,492,844	10,638,937	4,860,767
Total	64,840,459	27,620,206	17,979,150
Municipal Loans—			
Indian	1,178,500	985,000	Nil.
Colonial	4,455,551	3,878,306	745,293
Foreign	8,167,353	4,241,812	1,813,830
Total	13,801,404	9,105,118	2,559,123
Railways—			
Indian	5,303,875	6,674,250	400,000
Colonial	7,446,776	10,665,000	4,721,125
Foreign	40,033,278	34,213,311	29,428,120
Total	52,783,929	51,552,561	34,549,245

Foreign Capital Investments of Great Britain: Public Loans and Railways.

Miscellaneous—			
Banks	1,220,000	1,602,500	7,104,427
Breweries and Distilleries	Nil.	167,120	44,800
Canals and Docks	450,000	Nil.	400,250
Commercial, Industrial, etc.	9,343,862	2,639,852	2,468,111
Electric Lighting and Power	2,403,490	1,629,440	770,000
Financial, Land, Investment, and Trust	8,326,204	5,163,144	4,445,671

Miscellaneous Investments.

† Period from 1st July, 1908, to 30th June, 1909.

Miscellaneous Investments, continued.

	£	£	£
Gas and Water	1,218,822	519,500	280,000
Insurance	Nil.	Nil.	Nil.
Iron, Coal and Steel	1,521,840	736,050	387,547
Mines	7,951,887	3,634,764	6,752,705
Motor Traction and Manufacturing	80,000	145,000	502,000
Nitrate	164,700	566,750	790,000
Shipping	405,000	975,110	Nil.
Tea, Coffee, and Rubber	1,824,300	1,158,048	1,030,220
Telegraphs and Telephones	Nil.	150,900	8,286,250
Tramways	9,330,270	2,778,400	972,402
Total	44,240,375	21,866,578	34,234,383
Grand Total	175,666,167	110,144,460	89,321,901

Geographical distribution of Foreign Investments.

Let us now turn from the economic to the geographical distribution of our foreign investments. We have already outlined the theory which general considerations of economic forces suggest, viz., that capital will tend to seek its level as a productive agent, by finding out those countries where it can apply itself, with the requisite amount of security, in services of primary utility. For example, one of these primary services, perhaps the most important, is railroad making. The equipment of some large potentially productive area in Canada, Argentina, or China, with adequate railroads, is probably the

greatest service which British capital is capable of rendering, not merely to the country thus opened up, but to the world at large, and indirectly and in a particular degree to the industrial interests of Great Britain herself. A full exposition of this last statement, to some minds debatable, is reserved for the next chapter. It may stand awhile as an unproved economic dogma, here adduced by way of explanatory introduction to the actual facts of geographical distribution which I proceed to tabulate, condensing for this purpose Mr. Paish's estimate for the year 1910.

British Capital invested in Colonial Securities during one year.

Capital invested in British Possessions and in Foreign Countries, 1910:—

British Capital invested in Foreign Securities during one year.

Colonies and India.	Governments.	Municipalities.	Railways.	Other Securities.	Total all Securities.
	£	£	£	£	£
America ...	4,427,451	3,443,983	10,402,497	16,252,227	34,526,158
Australasia ...	6,442,074	520,217	570,000	2,648,140	10,180,431
Africa ...				12,950,222	12,950,222
Asia ...	9,863,750	487,500	3,100,000	11,404,538	24,855,738
Unenumerated				300,000	300,000
Total ...	20,733,275	4,451,700	14,072,497	43,555,127	82,812,599
Foreign ...	17,275,856	6,809,514	42,670,148	39,583,020	106,338,538
Grand Total ...	38,009,131	11,261,214	56,742,645	83,138,147	189,151,137

The more detailed Table summarised here under the single head "Foreign" yields information of great significance. First of all, we note the temporary revival of Europe as a field of British investments, though not upon a scale commensurate with the borrowing of the New World.

The most considerable European borrowers in 1910 were the following countries:—

	£
Austria	2,368,000
Bulgaria	3,603,600
Denmark	1,089,000
Greece	2,345,834
Hungary	1,950,000
Russia	3,936,655

Europe a modest market for British Capital.

Though the American borrowing is not nearly so large as in the previous year, it still represents an enormous preponderance, the United States once more taking its place at the head of the list, and rivalling Canada in the new capital it has absorbed, though it is considerably surpassed by the group of South and Mid American States, which took amongst them about £40,000,000.

Though railways are at present taking a smaller proportion of the capital invested abroad than was formerly the case, they still afford by far the largest single employment, taking in all £56,742,645, about eighteen millions of which goes into South American rails.

It will be useful to append the following list of the countries which, for the last year, have shown themselves our best customers in the investment market:—

British Capital absorbed by the Countries of the World.

	£
Canada	32,359,158
United States	32,237,294
Argentina	16,595,020
India	14,720,503

Brazil	10,988,686
Straits Settlements	9,286,337
Rhodesia	6,686,176
Dutch Indies	6,328,916
New Zealand	5,258,717
Mexico	4,946,139
Chili	4,684,661

Not one European Country, it will be seen, figures in the list. The large borrowing countries belong to two categories (1) the "new" countries of North and South America and of our self-governing colonies, seeking the aid of foreign capital for the development of huge sparsely-settled tracts of land; (2) old countries in Asia entering upon the ways of Western civilisation.

Two categories of Countries which utilise British Capital.

The general tendency has been in recent years for England to go further afield for her foreign investments, and to spread her holdings over a larger number of geographic areas. Both relatively and in some cases absolutely she has reduced her holding of securities in the older, more developed, countries, where capital is available largely from domestic sources and where interest is low. England was once a large holder of government bonds in various European states of which she now holds very little. Though, as we see, she still invests not inconsiderable sums in United States railways, her interest in these bonds and shares is no longer so paramount as once it was. Not only has the United States acquired an ever-growing share, but other European nations, especially France, Germany,

Decreasing amount of British Capital in United States Railways.

Holland, and Switzerland have considerable stakes.

Our dispersive investment policy has of course been favoured by two considerations, first the numerous widely distributed and profitable areas of investment offered by our Empire, especially India and the three self-governing groups; secondly, by the magnitude and variety of our shipping and our trading connections, which have brought us into more intimate relations with foreign countries needing capital than was possible for other European nations.

Aggregate of foreign Securities held in France in 1900.

But there is plenty of evidence to show that other European nations with investing power are beginning to follow our lead. Though the amount of foreign securities listed in the French Bourse is of course no index of French ownership, enquiries into trust securities held by the Bank of France, and into other avenues of information, led M. Neymarck to estimate that in 1900 the aggregate of foreign securities held in France amounted to about 31,200,000,000 francs. About three-quarters of this was in government bonds and similar securities, the other quarter in shares and bonds of Companies. The allocation of this indebtedness indicates, however, that French capital is far less widely distributed, geographically, than British. Comparatively little is placed outside Europe, and of that Egypt and three South American states, the Argentine, Brazil, and Mexico, take almost the whole. Her Russian holding is of course by far the largest, but to

Distribution of French Capital compared with British Capital.

Spain, Austria, Turkey, Italy, large sums are entrusted. Germany's foreign investment power is not only of later origin than that of France but it exhibits no signs of immediate growth, if we take for our guide the official statistics of Securities issued on the German Bourses. The following Table for the decennial period 1895-1904 indicates a diminishing foreign issue, though this conclusion must be qualified by the knowledge that a large and increasing quantity of foreign investments are made through bankers in London, Paris, and other financial centres of Europe.

German Capital: relation between Home and Foreign Investments.

	German Issue of Home Securities. Million Marks.	German Issue of Foreign Securities. Million Marks.	Percentage of Foreign Securities to the whole
1895 ...	1,056,72	317,90	23·1
1896 ...	1,327,56	568,27	30·1
1897 ...	1,328,51	632,91	32·3
1898 ...	1,697,43	709,72	29·5
1899 ...	2,377,57	233,82	8·0
1900 ...	1,575,74	275,27	14·9
1901 ...	1,421,31	210,03	12·9
1902 ...	1,657,19	453,50	21·5
1903 ...	1,271,50	241,67	16·0
1904 ...	1,756,72	232,11	11·4
	15,470,25	387,520	19·97

Difficulty of accurately measuring Foreign Investments.

The difficulties of measuring foreign investments with any degree of accuracy are, however, at present insurmountable. For instance, France, Italy, and Switzerland are more or less

permanent abodes of large numbers of wealthy foreigners who, though not members of the nation, are owners of securities. Again, in the case of Belgium it is impracticable to discriminate how much of the money invested there in foreign securities belongs to Belgians, and how much is French or German money driven to Brussels under the stress of high taxation and stringent bourse regulations at Paris and Berlin.

Europe increasing the Amount of its Capital distribution.

But while such considerations invalidate precise measurement, there can be no question but that every European country which is sufficiently developed to have a large surplus is advancing in the arts of cosmopolitan investment. When the habit of placing savings outside the immediate control of the owner is once established, the enlargement of the process proceeds apace. For French peasants first to put their savings into Russian bonds, or Suez shares, was a great adventure; after that it is comparatively easy to get money for American rails, or Transvaal mines.

Inducement to Capital distribution: a higher rate of Interest.

Of course, in the mechanics of these operations there will always remain a certain amount of friction to be overcome. Other things equal, it will be more difficult to draw money further from the base of ownership to comparatively unknown and so more speculative areas of investment. Expanding knowledge and experience, together with greater political security in backward countries, will, however, continually tend to reduce this friction, enabling near and distant investments to rank more closely in accordance with

their inherent merits, i.e., the real productivity of the capital. The mode of overcoming such friction as remains is of course a higher rate of interest. The net return upon capital invested even in the United States is somewhat higher than in Europe, while Brazil or Argentina, though now well established in reputation, so far as general security of property is concerned, must pay a normally higher rate for capital of equal yield and equal actual safety. As standardisation, economic and political, proceeds, these differences in net yield will diminish, larger portions of the world standing on approximately the same level as markets for investment. On such areas investment will tend to become less and less speculative. But there is no likelihood that the speculative element will tend to disappear. For two permanent causes will prevent such disappearance. In the first place a very large part of the richest natural resources of the earth, as yet scarcely touched, lie in tropical countries where the settled methods of political and economic administration known under western civilisation are not practicable. Secondly, even in those countries where good security of property and regularity of industry are available, the further process of investment will have recourse ever more largely to industrial and commercial businesses for the supply of needs, less regular and calculable in their quantities and kinds than those which are embodied in the staple industries

Impossibility of entirely Eliminating the speculative Element.

Irregularity of Industrial and Commercial Businesses.

first brought under company rule.* The higher is the standard of class or national comfort at which a particular want emerges, the more irregular it tends to be and the more precarious the industry which caters for it. While, therefore, increasing areas of investment tend towards a common level of attractiveness and productivity, new markets for capital of a more speculative character will continually be opening up, either in countries insusceptible of efficient political and economic control, or in industries for the supply of essentially capricious or fluctuating demands.

* This increasing irregularity of industrial and commercial investments may, however, be modified by certain effects of a more equal distribution of incomes. This consideration is discussed in Chapter VIII.

CHAPTER VI

FOREIGN INVESTMENTS AND HOME EMPLOYMENT.

As the saving and investing powers of a nation grow, by reason of improved methods of producing wealth, a larger quantity and a larger proportion of new capital tend to seek investment in foreign countries. Though it must be presumed that the owner of such capital gains by sending it abroad so as to earn for him a higher rate of interest than he could get at home, there are many who maintain that this private gain is attended by a public loss. For, if this capital had stayed at home and been applied in some home investment, it would, they urge, have given employment to British labour, and though the wealth it assisted to produce might be slightly smaller than that produced through investing it abroad, there would be caused an increased aggregate of industry and wealth-production in this country.

Argument against Foreign Investments.

Investment of capital abroad undoubtedly implies an increase of export trade. For in no other form than that of British goods can British capital go out. An English investor who buys shares in

an Argentina railroad company, or in City of Osakas, pays for these shares by money which is nothing else than an order upon British goods. Defenders of the utility of foreign investments sometimes make much of the fact that, by floating and investing largely in foreign rails or mines, we secure orders for British engines and machinery to equip these businesses, and for British ships to carry out their plant. And this, no doubt, is true, but it is not really relevant. From the standpoint of volume of foreign trade it makes no difference whether the Argentina railway, whose shares we take up, equips itself with British or with American engines and rails. For if Argentina does not take the subscribed capital in British-made railway plant, it must take it in other British goods; or, if it does not do this, it must cause some other foreigners to buy British goods instead of doing so herself. Only in one of these ways can a British investment in Argentina be effected. If the cheques with which British investors buy the Argentina stocks are converted into orders for British engines and rails, the nature of the investment is obvious. But if they are not so converted, it remains equally certain that the British indebtedness they register can only be met by inducing some foreigners to buy British goods, whether rails or cotton goods or ships or other products, which they would not have bought but for this British investment in Argentina stocks. How this compulsion to buy British goods is exerted

The case for Foreign Investments.

Effects of Foreign Investments on British Trade.

through the operations of international exchange I need not here describe. For no business man will dispute the fact that an investment of British money implies an export of British goods, not necessarily at once but ultimately, and usually at no distant date. The capital thus exported will earn a slightly higher rate of interest than it could hope to earn at home, and this interest will be paid in foreign goods which will come in to swell the import trade of this country. Even if the interest is not at once taken in imports, but is left to accumulate by reinvestment abroad, eventually the fruits of this enhanced foreign investment must be taken in foreign goods entering as imports.

Foreign Investments mean Increased Imports.

Now, those who think the free growth of foreign investments injurious to this country find three separate damages accruing from this process.

Charge levelled by Foreign Investment dissenters.

1. It reduces employment and retards industrial development at home.
2. It introduces an increasing quantity of imports which need no exports to pay for them.
3. It equips foreign competitors to compete with us in our own or neutral markets.

It is necessary to set out these charges in more detail before examining their validity.

An article in the "Bankers' Magazine" for November, 1909, upon "Investments, Exports, and Employment" makes the following com-

parison between the results of foreign and home investments:—

Foreign Investments and British labour.

"For the time, the effect of investments abroad has the same influence on the employment of labour in this country as of investments in the United Kingdom. Labour is set in motion, both to produce the exports and to transport them to the country to which the advance is made; the ships in which the goods are carried have to be built, manned, and kept in repair. But though this is the effect at the time, the eventual influence of a foreign investment on the employment of labour is very different, after the first year or so, from that of an investment within the four seas. When the investment is made in this country, it remains either as a productive instrument continually assisting our internal trade, in the shape of a railway, a new tramway, new ironworks, or it may assist the convenience and prosperity of the inhabitants in the form of waterworks or gasworks.

Home Investments and British labour.

These last may not produce a return in exactly the same way as a new manufactory does, but they add to the comfort of the inhabitants, as waterworks do, and they also enable many trades to be carried on which require a continual water supply. The same applies to gasworks, electric works, and many other similar concerns. If only a tenth part of our investment is in domestic undertakings, as appears

to have been the case in 1909, we cannot wonder at the increase of unemployment and of distress among the working classes."

Though the income derived from these foreign investments in the form of dividends may be somewhat larger than if the money had been invested at home, the expenditure of this larger income, it is contended, will afford a very slight stimulus to British industry and employment as compared with the application of the capital sum in home trade.

Trade depression and migration of Capital.

The reasoning at first sight seems plausible. Though, as statistics show, the general tendency to invest an increasing proportion of our capital abroad proceeds irrespective of the state of trade, it is accentuated in times of depression. But to charge the migration of capital with being a cause of home depression and unemployment is to transpose the true order of causation, putting the cart before the horse. An increase of foreign investment does not cause unemployment and depression at home; on the contrary, unemployment and depression, involving a reduced demand for capital at home, drives it abroad. It is important to establish the truth of the following propositions. 1. In periods of unemployment and depression in this country there is no lack of capital for home use. 2. If an attempt were made to stop capital from going abroad and force it into home investment, no nett benefit to home trade would accrue. 3. Foreign investments, therefore, constitute a useful means of disposal of

Capital Investment: three Propositions.

a surplus of British capital which remains after the needs of the home investment market are sufficiently met.

Sufficiency of Capital in time of Trade Depression.

The first of these propositions is the crucial one. For if, during a period of trade depression, there is no deficiency of capital, it is idle to argue that it is injurious for capital to go abroad. Now, is it not notoriously the case that, when a period of trade depression sets in, all the important trades of the country are amply supplied with all the capital they want and can profitably use?

Effect of employing Capital for Trade purposes.

So long as capital is treated in an abstract and vague manner as financial power, it may appear that pumping more of this power into a trade will stimulate its vitality. But those who follow this economic interpretation of investment will not be thus deceived. They will recognise that putting capital into a trade means supplying it with more buildings, machinery and other plant, more raw materials, fuel, and other concrete wealth required to co-operate with labour, and such money, or general command of wealth, as is needed to maintain labour until the goods produced by it are marketed. Now, can it be said that any of these forms of real concrete capital is lacking when trade depression sets in? Confronting the unemployed or under-employed labour is unemployed or under-employed plant and machinery, there is usually an abundance of raw materials, and warehouses are glutted with unsaleable goods; all the material apparatus for

making, carrying, and distributing goods exists not merely in sufficiency but in evident excess. Is it credit that is lacking? Though at the moment of a trade crisis there is a stringency in the money market with a high price for money, this is not the case during a depression. Quite the contrary; there is an abundance of money in the hands of bankers and other financiers, not merely for investment in any home business that shows promise, but for loans at low rates to manufacturers and traders who can give reasonably good security, i.e., who can show a probability that they can use the money to produce goods which can be profitably sold so as to enable the borrower to repay the advance he has received.

Trade Depression and the Money Market.

In the face of these notorious facts, how can it be contended that there is any lack of productive capital in a time of trade depression, or that foreign investments have robbed British industries of the capital required to keep them fully employed? The problem of a general depression of trade, like that of 1908-9, is the problem of a simultaneous excess of capital and labour, unable to co-operate for ordinary purposes of production because of an insufficient market for the goods they could produce. Every well-informed and thoughtful business man knows that the crux of the matter lies in the normal tendency of producing power to outrun the actual rate of consumption, so that periodically the whole productive machinery must be slowed down. It is no part of my business here to discuss the causes of

Causes of general Trade Depression.

this normal tendency towards over-production, or under-consumption.* For it is sufficient to point out the admitted fact that though in theory it should be as easy to sell as to buy, and consumption should always keep pace with production, in practice it works out quite otherwise. Consideration of the actual condition of trade in a depression precludes the serious entertainment of the suggestion that at such times there is any lack of capital in British industries. It is, doubtless, sometimes maintained that even in depressed trade there are some rising new industries insufficiently provided with capital. But those who put forward the hypothesis may be safely challenged to name the trades which at such times, when loanable capital is extraordinarily cheap, are unable to get enough for any reasonably profitable use. Though it is sometimes expected that cheap money will suffice to stop a general trade depression by stimulating production and extensions of businesses, there is no evidence that it does in fact so operate to any appreciable extent. Not until the slackening or stoppage of production has gone so far that surplus stocks are gradually cleared and consumption has begun once more to tighten up the reins of industry does a real demand for more capital in home trade become effective.

Excess of Supply over Demand the principal factor in Trade Depression.

Inability of Cheap Money to arrest Trade Depression.

This being so, it is idle to contend that hampering the process of foreign investment, by differen-

* It is discussed at some length in my volume, "The Industrial System" (Longmans).

tial taxation upon their dividends or by any other interference, would be beneficial to British trade and employment, or that it would bring into actual use a larger quantity of home capital.

Prohibition of Foreign Investments through taxation.

The desire to obtain the higher rate of interest yielded by foreign investments at such times must be deemed to be a necessary motive for the saving which has brought into existence the capital that seeks this investment. Any artificial impediment would then not simply divert this capital from foreign into home investment: it would stop the creation of this capital. But, it may be urged, this will only apply in part to capital that goes abroad. Much of this capital, it will be contended, would be willing to take a slightly lower interest at home, if it were not permitted or encouraged to go abroad. Now, what does this mean in terms of industry? It means that at a time when there are more cotton factories and iron foundries than are able to get orders it is proposed to build more factories and more foundries and equip them with plant; that when railway returns are low and traffic falling, more engines and rolling stock shall be provided and necessarily unremunerative branch lines be laid down; that when overbuilding has everywhere been going on, more buildings shall be put up, and so forth. Now, as we have already seen, this could not to any considerable extent take place. For bankers and other financiers controlling the course of new investment would not dare to embark upon such precarious enterprises at such

Excess of Capital for Home Investments.

times, would not dare to put up new mills on the chance of their cutting out existing mills in the competition for orders and contracts already insufficient to furnish adequate employment to the capital and labour in the trade. But suppose that, actuated by some reckless faith in the future they did invest their clients' money in new plant and other business undertakings at such a time, what would be the result? The immediate effect, I agree, would be a stimulus to trade: there would be more employment in the mining, machine-making, railway, building, and other trades engaged in setting up the new factories and other plant. But, seeing that the next effect would be an enhancement of the manufacturing and other productive power, which was already seen to be greater than could find regular, full, and profitable employment, it seems evident that any such addition to this productive power would intensify the malady, and that the temporary stimulus, given so long as the new plant was being set up, would involve an enlargement of the depression as soon as an attempt was made to operate the new manufacturing power. For if the productive power already existing was found to be so much in excess of what was wanted to supply the markets, an increase of this power would glut the markets earlier and more completely. So an artificial stopping of home industries would cause more violent disturbance of the industrial system, involving bigger and more injurious stoppages,

Reckless employment of Capital in Home Industries.

Home Industries: effect of over-production.

and adding nothing to the aggregate of trade and employment over a term of years.

Put more simply, this argument means that foreign investments do not injuriously compete with home investments, robbing the latter of capital which it could put to advantageous use in employing British labour, but that they represent a use found abroad for a surplus quantity of British saving, which otherwise would either not exist at all or would represent a wasteful over-supply of home capital. It is no reply to say that there are new electrical, motor car, and other home industries ready to absorb any amount of new British capital in developing new industries for the stimulation and supply of new wants. These new trades can already get as much capital as they deserve or can absorb: interference with foreign investments would not enable them safely or advantageously to increase their pace of growth.

Foreign Investments represent surplus British savings.

Foreign investments, then, form in the first instance a safety-valve against excessive gluts of capital at home. They find a profitable use for capital which otherwise could not economically fructify at all. The profits of this use come to this country in the form of exports. This brings us to the second grievance of the critics of foreign investments. They find in the goods which come into this country in payment of interest on foreign investment an additional injury to home employment. For, whereas other imports are the means by which foreigners pay for British goods which go out to them in export trade, these imports

Profits derived from Foreign Investments.

draw forth no such exports, and so stimulate no corresponding activity in British industries. The receipt of some £120,000,000 worth or more of such free goods into our markets, however desirable from the standpoint of the consumer, inflicts, they hold, upon the producer two injuries. In the first place, there is the negative injury that he has to send out no goods to pay for them; in the second place, they displace to some extent goods which would have been produced at home by British capital and labour—a positive blow to British industry. The investment of British capital abroad is thus represented as responsible to a larger extent than any other cause for the "dumping" on our shores of large quantities of goods which could and would otherwise have been made at home, employing our capital and labour in their making.

Objections of the anti-foreign Investor.

Nor is this the worst. The exportation of capital not merely brings this influx of unpaid-for imports, but, by improving foreign countries and equipping them with our best machinery and plant, it makes them formidable rivals of our own producers. Even if it be admitted that the development of the agricultural resources of such lands as Argentina and North-West Canada is justified, in bringing us the abundant supplies of grain needed by a population which, like ours, must supplement its native resources from foreign lands, it cannot be equally serviceable to build up competitors for our manufactures or our carrying trade. With capital that we ourselves supply,

Further objection: trade competition.

countries such as the United States, Japan, and India, not to mention countries nearer home, are enabled, first, to produce for themselves manufactured goods which we used to sell and still would like to sell them ; secondly, to compete with us and often to displace our wares in neutral markets; last, and worst, to invade our own markets and to undersell our manufacturers. Such are the further counts of the indictment against foreign investments as enemies of home trade and employment.

Final counts in the Indictment.

Before answering them I may remind readers of the curious dilemma with which they seem to be confronted. We have already proved that the capital that goes abroad is not wanted and cannot, in fact, be utilised at home. It now appears that it is even more injurious to our trade if it be allowed to go abroad. Only two other courses seem open, either not to bring it into existence or to sink it into the sea. But before adopting such counsels of despair we will examine more closely the damages which these investments are said to inflict upon our trade.

These large quantities of imports, due directly and indirectly to foreign investments, are obviously advantageous to our consuming public, whose real incomes are thus raised by the lower range of prices caused by these accessions to our home supplies. Since the final object of all industry is to put consumable goods in the possession of consumers, it may be claimed that this

Foreign Investments benefit the British Consumer.

admission is in itself a sufficient defence of the beneficial nature of foreign investment.

Foreign Investments in relation to Home Trade and Employment.

But we may be reminded that we are here arguing the issue from the standpoint of the volume of trade and of employment, and that in such an argument the consumers' interests have no relevancy. Let us then return to the immediate question, viz., whether the foreign investments cause a reduction in the volume of home trade and employment, first, by displacing home-made products in our markets; secondly, by displacing our products in foreign markets.

Trade depression not caused by Investment of Capital abroad.

Now, in the first place it must be remarked that if foreign investments exercised this depressing influence upon home trade, we should expect this depression to be permanent and of increasing intensity, to correspond with the growth, both absolute and relative, of this employment of our capital. For the quantity of imports entering this country as interest upon our foreign capital continually grows, and so does the competing power of foreign nations due to the stimulation of the capital which we provide them. Yet for considerable periods our capital and labour in home industries do not seem to suffer from this invasion, but are able to put forth their full activity in profitable industry. Nor is there any evidence that trade depressions and unemployment are increasing in frequency or intensity in this country, as might be anticipated if this artificially stimulated foreign competition were their cause.

But this consideration does not in itself dispose of the case against foreign investments. For it might be that this depressing tendency was only realised when a financial crisis, bad harvests, or some other cause, was weakening our markets. It is necessary by direct analysis to face the question whether foreign investments can and do damage our powers to produce and to market our products. Now, here it is material to point out that a very small proportion of our imported goods, whether coming as interest on capital or in ordinary course of exchange, consists of fully manufactured or completed goods, ready to pass into consumption without any use of British industry. More than three-quarters consist of foodstuffs, materials, and partly manufactured goods. These, entering as raw materials into many of our staple trades, by their abundance and their cheapness keep down the costs of production of the final products, and by lowering the prices enable us to effect larger sales at home and to secure large foreign markets which we could not have done but for the assistance of these imports. Even of the 23 per cent of imports classed as mainly or wholly manufactured goods a large proportion figures as "costs" in some home business. Foreign door-frames or window-sashes cheapen the cost of building and so cause more or larger houses to be built, thus compensating for the loss of home employment which appears to be inflicted on our carpenters. Even such articles as rolled desks and bicycles are not

Bearing of Foreign Investments upon Home Production.

How imports benefit Home Production.

mere consumers' goods: they figure as "costs" in large numbers of productive and distributive trades: to keep them out would mean some lowering of profits or raising of prices for British made products.

Economy of free importation.

Nor can we ignore the important effect of free importation upon real wages. By helping to keep down the price of foods and of all other consumers' goods, manufactured or other, imports tend to keep down money wages, and so to maintain a lower range of selling prices than would otherwise be possible. This economy is applicable to all British trades, but its most important effect consists in enabling us to secure large and profitable foreign markets, underselling nations which by tariffs, or by lack of imports entering as interest on foreign capital, are subject to higher costs of production.

Foreign Investments benefit Home Industries.

This defence of the economy of free importation shows that the goods which enter as interest on foreign investments cannot be regarded merely as displacing goods which would otherwise have been made by British industries. Their main effect appears to be stimulative rather than depressive, enabling our industries to turn out larger quantities of goods at lower costs and prices for our own markets and for export trade.

This primary economic effect of foreign investments is supported and enhanced by a no less important secondary effect. The main economic object and result of our exportation of capital is to exploit the natural and human resources of

relatively backward countries. By making roads for them, developing their mines, fields, and forests, and in due time supplying them with machinery and other plant for a manufacturing career, helping to build and equip their cities, and to train and organise an industrial population, we are undoubtedly raising them towards the same industrial level as ourselves. Are we, thereby, setting up dangerous rivals who will rob us of our trade, in their market, our market, and neutral markets? The hypothesis which underlies this notion is that there exists at any time only a limited amount of market, and that increased sales effected by one competitor imply a corresponding decline in the sales of another. Now this conception of trade is fundamentally false. The first principle of trade, national or international, is that of co-operation, or mutual service, not of rivalry or antagonism. The process of competition is subordinate to co-operation. Absorption in the concrete details of a single trade tends to hide this truth, and has enabled certain persons to represent the relations between trading nations as essentially hostile. The fallacy here is double-rooted. There is first the false assumption that nations as such are economic units, and trade with one another and with other nations. Great Britain, Germany, and the United States are not trading firms; they do not bid against one another for custom; there are no commercial relations, except of a subsidiary and indirect kind, between them. Certain English firms compete with

Economic objects of Capital invested abroad.

Co-operation the first principle of Trade.

certain German and American firms in the markets of these or other countries. So far, however, as such competition involves rivalry and antagonism, it is much keener and more persistent between the several English or the several German firms than between the members of different nations.

Advantage of equality of business ability.

The second form of the fallacy is the supposition that it is an advantage for a business man to be surrounded by other business men less prosperous, intelligent, and enterprising than himself. At first sight it may look as if he were the gainer by being so much better off. But this is not really the case. An enterprising and productive man needs neighbours who are enterprising and productive, and that for two reasons. There are many things he wants to buy, and many that he wants to sell. He can buy to the best advantage if his neighbours engaged in various industries are as keen, as enterprising, and as productive as himself. Similarly, he can sell to best advantage if the growing needs and desires of his neighbours are fortified by purchasing power. Every business man knows that it is better to be a member of a prosperous industrial community than of a poor and backward one. What applies to a small applies likewise to a large community. The merely political barriers of States have no power to annul or to restrict this economy, the advantage of having large numbers of rich and prosperous neighbours. No doubt every individual trader would like to be the only

Mutual prosperity essential in business.

prosperous trader in his particular line, and to have large numbers of prosperous neighbours in other lines. But this condition he cannot realise, and if he could it would not really be to his advantage, for it would remove that healthy stimulus of competition essential to industrial progress.

Competition and co-operation in business.

If, then, it be admitted that an English firm gains by having plenty of other prosperous firms all about the country, even though some of these firms are in its own line, similarly it gains by having prosperous firms in other countries from which to buy and to which to sell. In other words, the detailed antagonism of competitors in one's own trade is a consideration subsidiary to the gain of having the effective co-operation of prosperous businesses in other trades.

This is only another way of saying that trade is a mutual exchange of goods and services, and that it is better to have a large number of rich persons with whom to carry on exchange than a small number of poor ones.

Foreign Investments increase Trade operations.

Once expel the fallacy that nations are trading units, the application of the doctrine to foreign investments becomes obvious. For foreign investments are a means of enlarging the circle of business men capable of supplying what we want to buy and of demanding what we want to sell. The fact that some of these business men get business away from us is a comparatively small and incidental drawback to this great economy arising from an effective expansion of the area of prosperous exchange.

The interest which comes back to this country from foreign investments is not the only great gain which comes to the members of our nation from this process. The opening up and development of North and South America, of India, Australasia, and of other countries which have sucked up our surplus capital, has meant an enormous increase in the incomes derived from our home industries and in the purchasing power of these incomes. In the development of these countries by our capital we are building up new customers for our goods and new sources of supply for what we need to buy. As they thus develop, they will display powers to supply to themselves, to us, and to the world, certain sorts of goods better or more cheaply than we can, so driving our home industries gradually out of these branches of production into others that yield products which enable us to buy from them upon terms more advantageous to us, the goods we formerly produced. The notion that there is a limited number of trades, each of a limited size, and that, therefore, if by developing another country we lose some trades or diminish the size of them, we are damaged in the aggregate of our national industry, is a fallacy based upon an ignorance of the very nature of trade as an exchange of goods for goods. Under modern conditions of the interdependency of nations in world-trade, it is impossible for any nation to use its improved development and richness of resources so as to injure the aggregate industry and employment of

Development of Foreign and Colonial Trade by exportation of Capital.

Interdependency of Nations in World-trade.

any other country in commercial relations, directly or indirectly, with it. Least of all is it capable of injuring the industries of that country whose capital has helped to develop its resources and with which it is compelled by economic necessity to maintain close relations of exchange. On the contrary, a country, thus developing, cannot keep its gains entirely to itself, but is forced by sheer self-interest to communicate large parts of them to those who buy from it and sell to it. Canada and Argentina might like to keep for their own farmers the full benefits of the rich virgin wheat lands opened up by British capital. But they are compelled to give us a considerable portion of the benefit by cheapening the price of wheat. And so it is with every sort of wealth produced in these new countries: the competing farmers, transport companies, and dealers in these countries, by the very process of seeking markets for their goods, are obliged to hand over a large share of the gains of the development, not merely to the foreign capitalists in interest, but to all those groups of foreign producers and consumers, who have dealings with them. It is not even necessary that our people should have direct dealings with a foreign country to which we have lent capital, in order to profit by the development due to our investment. We might, for instance, in the not distant future find some parts of China a very favourable field for investment. But China might not by this development be able to sell us any large quantity of goods we wanted, or

Mutual advantages of Capital invested in foreign Countries.

How the distribution of profit is effected.

to take from us any large quantity of what we have to sell. Even the interest upon the capital they might pay us, not in Chinese wares, but by orders on the goods of Japan, America, or some other country with which they did large trade. But the development of China thus procured might none the less be immensely advantageous to British industries, by furnishing cheap foods or materials to foreign producers in the United States or some other country which was thereby enabled and obliged to sell to us materials or goods which we want for our use on terms advantageous to our industries.

Home Industries and Foreign Development.

Our relations with South Africa illustrate this important truth, upon one side. Though South Africa is a not inconsiderable purchaser of our manufactures, she has comparatively little to give us that we want. The gold and diamonds which are her chief products for export do indeed pass through our hands, but we do not keep or want to keep the bulk of them for our own use. We retain comparatively little of the fruits of the mining and other work our capital has done. The bulk of the interest due to us, of the payment for the British manufactures they buy, and of our share in the general wealth of the country, comes home to us in the shape of foods, materials, and manufactured goods from other countries which among them take the larger share of the gold, diamonds, and other products with which South Africa enters the world market.

How South African development affects Home Industries.

The development of a backward country by

foreign capital is always beneficial to the country itself, to the industrial world at large, and to the investing country in particular. It is of course quite conceivable that the greatest gainer, next to the developed country, might be not the investing country but some other in closer trade relations with the former. But for the barriers mutually established between Canada and the United States, the industries and people of the latter country would probably have reaped a larger benefit than the people of this country by the large influx of British capital into the Dominion. In the long run, indeed, they must be the greater gainers, though doubtless a large share of the gain may be attributed to work done or assisted by their own exported capital.

Benefit to the Investing Country.

But, normally, the people and industries of the investing country stand to gain more than any other foreign country. For in the first place, a large part of the concrete capital which goes out by the process of investment usually consists of engines, rails, machines, stores, and other equipment, ordered directly from firms in the investing country. Part, at any rate, of the management of the railway, mine, irrigation works, or other businesses to which the capital is devoted, is likely to be in the hands of persons belonging to, or friendly to, the investing country. Thus the work of repair, improvement, and extension in the future, will evoke fresh orders for the investing country. Moreover, the business and social intercourse involved in these proceedings will be likely

Investing Country the chief gainer by exportation of Capital.

to extend to others: business breeds business and every order smoothes the path for another order. Great Britain in particular has profited by this natural process: her generally sound and reliable goods, especially in the engineering and machine-making trades that figure so largely in the supply of concrete capital, have all over the world helped to pave a broad commercial road for other British manufactures.

Great Britain's supply of concrete Capital.

The indictment of foreign investment as an injury to home industry and employment thus completely breaks down on examination. The gains to the investing nation are four; first the export trade involved in the process of investment; secondly, the stimuli and food to home industries from the payment of interest, most of which comes in foods and materials that lower the "costs" of production in home industry, thus enlarging the home market, and the general export trade; thirdly, the share of the new wealth proceeding to her from the debtor country, directly and indirectly, by the ordinary processes of exchange; fourthly, the special trade relations set up and maintained by the very nature of the financial assistance rendered.

Four gains to the Investing Country.

The aggregate of these gains forms an immense positive advantage to home industries and home employment arising out of foreign investments.

CHAPTER VII

POLITICAL AND SOCIAL INFLUENCES OF CAPITAL.

AS the area of investment widens for any class or nation of investors, their interests and sympathies expand, and the influence they exert through public opinion or politics upon the conduct of affairs in the places where they have invested capital becomes a factor of growing importance. Regarded merely as an educational influence, this expansion of the area of investment is of considerable efficacy. A man whose business interests are confined within his parish is parochial in his sympathies and outlook. If, on the other hand, his trade brings him into touch with business men in many other towns in his native country, his country means more to him—he is a better citizen. Still more is this the case where trading interest is supplemented by investment and a business man has a "stake" in a number of industries in various places. Though his patriotism may be too much a matter of pocket and his politics too exclusively capitalistic, it remains true that they will be broader, and

Local influence exerted by Investors of Capital.

more intelligent, and on the whole more conformable to public welfare than the feelings and the policy of the mere parochialist. When trade and investments carry men still further afield, inducing a knowledge and an interest in the affairs of foreign countries, the widening of outlook and of sympathy involved lays the basis of the cosmopolitan, the true "man of the world." This expansion of interest and policy is essential to the success of the modern art of investment, and its political and social implications are of the first importance in the history of modern civilisation.

Essentials to Success in modern Art of Investment

For the members of one nation who have invested capital in a foreign country possess an interest in everything that may happen in that country to affect the security and the fructification of their capital. So far as any capital they may have invested in their own country is concerned, they can, as individual citizens or by combination, exert an appreciable and definite influence in protecting and improving it, where governmental means can be utilised. Though business men who cleave too closely to the principle "Our trade, our politics," may be dangerous citizens, working for a trade, or a class interest in opposition to the welfare of the nation's, their intelligence and influence will serve upon the whole to safeguard and advance the productivity of capital. Apart from the special trade interests which the pull upon a tariff or some particular policy of public expenditure may involve, they will be supporters of good order, education, and improved

Influence of the Home Investor on the Productivity of Capital.

efficiency of labour, and public development of the natural resources of the country. This would be the normal attitude of the enlightened capitalist with investments of various kinds in different parts of his own country.

Now the cosmopolitan investor will have the same interest in the good order and development of the countries where his capital lies. But not being a citizen of those various states he will not be able to exert the same sort of direct influence. Thus, as the numbers of these cosmopolitan capitalists grow and their stakes in countries not their own are larger and more various, the urgency of building up some international political machinery for protecting and promoting their scattered interests becomes continually more evident. So far as foreign investments depend for their safety and success upon local conditions affected by government there will be a constant growing tendency for investors to seek to influence that foreign government, either privately or by the diplomacy or force of their own government. Examples of such private intervention are the numerous cases where foreign syndicates obtain concessions for railroads, mining or other enterprises by personal negotiation with the government of a country without the assistance of their own government. The history of the Transvaal and Rhodesia, of China, Egypt, Persia is full of modern instances of private capitalistic negotiations with foreign governments.

Necessity of adequate Protection for Capital invested abroad.

Methods of obtaining Concessions from Foreign Governments.

But in recent times investors more frequently

utilise the diplomacy of their government to assist them in their negotiations for such concessions, and the course of foreign politics, especially in the Far East and in South America, turns more and more upon this competition of the pressure of foreign governments on behalf of groups of investors. Where investments have been thus effected, whether with or without governmental aid, the foreign stake in a country is always liable to involve the intervention of a foreign government if the security of the invested capital is threatened by alleged misgovernment. Sometimes, indeed, the pressure of investors has taken shape in private force for the substitution of a government more amenable to their management. This has usually happened where foreign investments have been accompanied by a considerable migration of foreign residents directly interested in the capital. The classical instance of such an operation in recent times is the Jameson raid. But the whole history of the Transvaal during the decade preceding the South African war is illustrative of the pressure brought to bear upon a foreign government by private groups of financiers for the protection and improvement of their investments, mostly by personal negotiations with ministers, but partly by diplomatic pressure of the European governments.

Political influence of Investors in Foreign Countries.

The Transvaal and financial pressure.

As foreign trade and foreign investment advance it becomes a more important and more useful function of every government to try to secure for its citizens new markets for their goods

and for their capital, and to employ public diplomacy and force to improve the markets already got and the capital already invested. As a number of civilised nations enter more largely and on more equal conditions into foreign trade and foreign investments, the foreign policy of their governments is more directly and consciously engaged in looking after these commercial and financial interests. Not merely are definitely commercial treaties formed to further these interests, but the political relations between nations are influenced, often predominantly, by considerations of finance. Russia's political alliances, to name a notorious case, have been dictated in the frankest manner by the necessity of public loans.

Political relations of Governments influenced by financial considerations.

But, where the borrowing country does not rank on a political level with the creditor country, the more usual case, the investment bond commonly leads not to an alliance but to some closer political control. Where the citizens of a powerful advanced state have invested largely in a weaker backward state, either in its public funds or by way of private enterprise, there constantly arise opportunities for the investors to press their government to interfere with the government of the backward state on their behalf. The properties which represent these investments may be actually in jeopardy, the foreign government may refuse adequate protection or may even confiscate the capital. In such cases it is recognised that the government whose citizens are thus plundered will intervene, if it has the power to do so.

Government intervention on behalf of Foreign Investors.

Where no such actual peril exists, there is a natural tendency by misrepresentations to secure the intervention of a strong government, if it is believed that the financial value of the shares will be thereby enhanced.

Desire for Imperial Expansion the outcome of Investment.

The growing practice of the government of strong advanced capitalistic nations to engage upon the modern process of imperial expansion is chiefly explained by the pressure of the investing classes for larger and safer areas of profitable investment. Other motives co-operate, the impulse towards emigration and the natural desire to keep emigrants under the flag, the desire for secure and preferential markets for the export trade, for mere territorial aggrandisement, or the mission of civilisation. But the main driving force which leads strong modern states to assert political influence and control over weaker states is the bond of financial investment. As the pressure of surplus capital beyond the national confines becomes greater and proceeds from a number of national sources, the use of its government by each national group of investors becomes more exigent and the competition for the best investments more keen. So we see all over the world, but particularly in Asia, foreign policy turning more and more upon the acquisition of spheres of preferential exploitation for railroads, banks, and other development work. By diplomacy, menace, and, in the last resort, by force, each government strives to obtain a "proper share" of each new field of exploitation for its own in

The bond of Financial Investment.

vestors. Egypt, Asia Minor, Persia, China, S. America, are primarily fields of investment, and the foreign politics which have relations to such countries are primarily determined by the financial considerations which lurk in the background of every national policy. Though other factors, dynastic, racial, religious, humanitarian, overlay and often conceal the play of financial motives, no candid student of the forces which have brought the countries named above into the sphere of interest or control of Western Powers can hesitate to trace the determinant acts mainly to financial causes.

Financial considerations the principal factor in Foreign policy.

At first sight this appears to imply that foreign investments are of necessity a disruptive influence, making for war. On the one hand, they incite strong advanced nations to bring within their political control, as spheres of interest, protectorates, or possessions, those weak and backward territories where their investors have acquired a heavy capitalistic stake, using whatever force is necessary to compass this imperialistic end. On the other hand, they appear to engender enmity and strife between the Powers which eye with jealousy the financial preserves seized by one of their number, and are driven to bitter diplomatic quarrels over each new promising area of investment that shows on the financial horizon, Morocco, Persia, Manchuria, China. "Modern wars are almost all for markets" it has been said, and if we lump together commercial

The possibility of National conflict through Foreign Investments.

and financial interests, it is not far from the truth.

This bellicose interpretation of investments seems also to be supported by the large part played by governmental loans employed to finance armaments and actual wars. No backward state, however large in territory and in population, could engage in a first-class modern war, or make the necessary preparation for it, without the use of international credit. The urgent need of such credit has been, as we have seen, a chief guiding influence in the foreign policy of Russia. The machinery of national and international investment appears to feed the war-spirit among nations by enabling them to furnish themselves with more gigantic and costly instruments of war than they could provide out of the current public revenue, and to wage wars upon a scale only rendered possible by the elaborate mechanism of modern credit.

Government loans for war purposes.

Thus it would appear that investment, like commerce itself, instead of being a bond of peace, may be a source of strife between nations. Cobden too confidently held that growing commercial intercourse between the members of different nations must soon make war impossible, because the injury to both nations attendant on a breach of peace would be so obvious. The "fight for markets" did not enter his mind as a possibility. So it might seem that the naturally pacific tendencies of international finance can be perverted into incendiary forces. Indeed, international finan-

Cobden's mistaken view regarding international commerce.

ciers are sometimes represented as ghouls egging on weak but ambitious governments with tempting loans to furnish themselves with warships and to embark upon perilous careers of aggression.

There is without doubt a large element of truth in these representations of the aggressive and provocative influences of international investment. Though war is nearly always injurious to the economic welfare of both nations that engage in it, there may be groups of capitalists within these nations, or in other nations, who stand to gain by the expenditure which wars involve. Though the South African war cost our nation enormous sums, a few groups of mining shareholders calculated they would gain by it, and a very few perhaps did gain.

Economic welfare of nations retarded by Political Disturbances.

Indeed, it is not right to shirk the peril involved in the unstable and irrational relations which subsist between public and private finance. So long as private investors who have put their capital in an ill-governed and insecure country at rates of interest which discount the insecurity are enabled to induce their own government to spend the public money in order to force a better government upon the country where their investments lie, the pressure of bondholders will continue to be a source of war. So long as valuable new areas of investment are practically kept by governments as special preserves for companies of investors exclusively belonging to the nation with political control, such finance will be provocative of strife between nations.

Causes of national contention.

These are the defects and dangers attending the development of modern finance up to the present stage. But the new and growing tendencies of a genuinely international finance must continually tend to diminish them and to substitute pacific motives. Though Cobden was too optimistic in attributing to the growth of foreign trade so early and so complete an efficacy as peacemaker, he was correct in his judgment of the tendency. A large and regular trade between members of two nations does modify the temper of their governments; a nation hesitates to seek to injure a good customer or to deprive itself of a good market for the articles its members need for home consumption and home industries. This genuinely pacific influence offsets, perhaps exceeds, the friction which may arise where the traders of two countries seek through their governments to secure a monopoly or preference of some neutral market. But the cross ownership of capital involved in international investment is a far stronger and steadier pledge of peace. When a group of investors, all members of a single nation, England or Germany, or the United States, puts a large amount of capital into developing a backward or an insecure country, this sort of foreign investment may induce an act of aggression or imperial expansion with the object of improving the investment, by obtaining political control over the country in question. But, even here the tendency will always be to

Flourishing trade the desire of every nation.

Cross ownership of foreign invested Capital.

gain their end by diplomatic or other pressure short of war.

Where the international character of an investment has been further marked by the substantial participation of investors of several nationalities, there will not be either the same temptation or the same ability to induce a government to bring pressure upon a foreign state in the interest of financiers, many of whom are not its own subjects. It is true that occasionally co-operation of several Powers, acting in the interests of international finance, has been attempted in China, Venezuela, and elsewhere. But the absence of a close identity of interests, indeed the probability of conflicts of interest between the co-operating Powers, makes for pacific settlement. It is evidently not the interest of a creditor country to inflict upon a debtor country the enormous material injuries involved in modern war. While, therefore, some grave insult or some policy of confiscation practised by a debtor country may still bring a forcible intervention of the creditor country, the international distribution of financial interests renders even this less feasible.

Government pressure in the interest of Financiers.

An illustration of this is furnished by the easy way in which the United States, by a firm parade of its Monroe doctrine, was enabled a few years ago to stop the several European governments whose subjects had interests in Venezuela, from applying force to collect their debts.

The Monroe doctrine in operation.

The Monroe doctrine itself, indeed, has been transformed in a most interesting manner from a

political into a primarily financial policy. So far as South America is concerned, it signifies that the United States furnishes a partial guarantee for the security of foreign capital invested in the southern republics, by undertaking the exclusive duty of keeping public order and inducing would-be recalcitrant creditors to "pay up." Though this obligation has political implications as well, it is primarily economic, tending to mark out large tracts of South America as special fields for American investment. But this financial protectorate, thus asserted by a first-rate power, will certainly assist the general development of South American resources through international finance, and by securing these states against such filibustering expeditions as that of Napoleon III. in Mexico, or against the political ambitions which Germany might otherwise have been led to entertain, it will tend to keep the peace over a large and a turbulent section of the world in which European investors are very largely interested.

Monroe doctrine and the security of Foreign Capital.

Recent developments in the Far East are making against the marking out of separate spheres of trading and exploiting influence in China and Manchuria for the traders and investors of the several European nations, which was the accepted policy of the nineties. For though the government of each interested power—Russia, England, Germany, France, and the United States—still manœuvres for railway and mining concessions for its own syndicates, there is no longer any hope of the break-up and parcelling-out

Trading spheres of the Far East.

schemes of the period before Japan became a recognised power. The new diplomacy for the development of Manchuria shows constant new shifts and combinations of political and financial bodies. The recent business arrangement between Russia and Japan for carrying forward a comprehensive railway system, if successful, would furnish a constantly solidifying basis of peace between the two hitherto opposed aggressive powers, while the finance for such a project would of necessity engage the co-operation of other European nations. For neither Russia nor Japan can find the requisite capital out of its own resources. The opposing policy, in which the United States has taken the lead, aiming at the construction of railways by an international syndicate, though defeated for the moment, probably represents the line to which events point in the future, not merely for Manchuria, but for the larger Chinese problem, which ranks as the greatest capitalistic proposition of the near future.

Effect of the Russo-Japanese railway scheme or. Foreign Capital.

The political break-up of China is no longer indicated as a probable event. On the other hand, the rapid strides made in education and in the study of western sciences and arts is a sure precursor to great economic changes, involving an organised endeavour to discover, develop, and use the vast mineral resources which certain Chinese provinces possess, and to construct the modern roads and manufactories which shall bring this vast population into the ring of civilised industrial nations. Though it is tolerably certain that in

Important economic advance in China foreshadowed.

this work the business of administration will be in the hands of the Chinese, the Oriental people best adapted to a business life, the initial operations of finance for some time to come must involve a large flow of capital from Europe and America. While the United States, in her new capacity of foreign trader and investor, turning ever more consciously to the Pacific for markets and investments, will probably apply a forceful diplomacy to secure Asiatic business for the financial groups who govern the great republic, neither they nor other western peoples will be able to pursue a selfish national policy very far. For when world-confidence in China as a field of investment is once fairly established, the suckage of capital will involve international finance upon a larger scale than has ever yet been practised. This large joint interest will afford the surest basis of peace, at any rate for a generation, in the Far East. Though other motives, non-economic, may eventually bring about an organised endeavour to expel western control, financial as well as political, from the Far East, and to revert to a separatist civilisation, a prolonged utilisation of western capital will afford the strongest guarantees of a period of pacific development, in which all the creditor nations of the world will take their share of profitable exploitation.

China the future area for Capital Investment.

International finance in the Far East a guarantee of Peace.

Imperialism, therefore, regarded as political domination of lower or backward peoples, primarily impelled and directed by desire for profitable trade, or in more recent times for profit-

able areas of national investment, is changing its character, especially in relation to South America and the Far East, the two most important fields of financial exploitation. The distinctively political and nationalist aspect is weakening and giving way to an economic internationalism exercised with very little direct assumption of political control, the minimum in fact that is found necessary to afford good security for the international assets.

Imperialism and Foreign Investments.

The entrance of the United States to a front place among foreign investors will probably consolidate this tendency. For the early experiments in American imperialism have proved neither profitable nor popular, and though governmental pressure may be carried far in order to prevent the closing of foreign areas to American trade and capital, it is unlikely that the United States will enter on any further scheme of territorial aggrandisement. A more or less formal coalition of American republics under the hegemony of the United States, and a naval policy in the Pacific, confined to the maintenance of an open door for American goods and capital, appear to express the present interests and aspirations of the ruling forces in the United States. This milder imperialism is of a definitely pacific character, likely both to promote good order and development among the backward nations and to assuage the jealousies of the great powers. Unless some reckless racial animosity should overpower the operation of these economic motives, Great

Foreign Investment policy of the United States.

Britain and the United States, directing their efforts primarily to freedom and security of investments in these great areas, will act as the leading channels for a finance which will become continually more cosmopolitan, so far as the ownership of the capital is concerned. Thus, we recognise how, in the relations between advanced and backward nations, the possession and utilisation of capital, placed by members of the former in the countries belonging to the latter, makes more for peace and good government in proportion as the finance grows more distinctively international.

International finance the path to peace and Government efficiency.

Not less striking is the pacific tendency of finance in the relations of the advanced nations themselves. In a very striking book entitled "The Great Illusion," the author dwells upon the revolutionary change effected in the motives and results of war by the advance made in recent times towards a financial solidarity of interests among the capitalist classes of the leading nations. For the successful army of a European country to invade a neighbouring country in order to raid its treasure, destroy its fixed property, and kill its industries, would not merely be a bootless policy, it would be a suicidal one. For the damage it would inflict upon the finance, the industry, and commerce of its own people, would be only second in extent to that inflicted on the enemy.

Peaceful v. warlike methods in Finance.

Suppose a victorious Germany army landed on our shores, proceeded, after ancient usage, to march on London and to loot the cellars of the

Bank of England, the only substantial treasure in the country,

"What would be the result of such an action on the part of a German army in London? The first effect, of course, would be that, as the Bank of England is the banker of all other banks, there would be a run on every bank in England, and all would suspend payment. But simultaneously, German bankers, many with credit in London, would feel the effect; merchants the world over, threatened with ruin by the effect of the collapse in London, would immediately call in all their credits in Germany, and German finance would present a condition of chaos hardly less terrible than that in England. It is as certain as anything can be that, were the German army guilty of such economic vandalism, there is no considerable institution in Germany that would escape grave damage; a damage in credit and security so serious as to constitute a loss immensely greater than the value of the loot obtained. It is not putting the case too strongly to say that for every pound taken from the Bank of England German trade would suffer a thousand. The influence of the whole finance of Germany would be brought to bear on the German Government to put an end to a situation ruinous to German trade, and German finance would only be saved from utter collapse by the undertaking on the part of the

Effect on British finance of a German invasion of England.

Effect of German invasion on its own finance.

German Government, scrupulously to respect private property and especially bank reserves."

Nor would the effect of extorting a heavy war indemnity be fraught with much lighter risks and damages to the victor. Suppose England to have vanquished Germany and to be in a position to extort from her the full costs of such a war:

Financial result of raising a War Indemnity.

"What would be the financial effect throughout the world of draining Germany of, say, five hundred million pounds in gold. In the attempt to secure this gold widespread and ruthless borrowing would have to take place on the part of German financial institutions. The bank rate would go up to such an extent that the recent Wall Street trouble would not be a circumstance to it. But a 7 or 8 per cent bank rate, prolonged throughout Europe, would involve many a British firm in absolute ruin, and a general loss enormously exceeding five hundred million pounds. Such would be the condition of things throughout the world that the leaders of finance in London, which is the financial centre of the universe, would, it is absolutely certain, throw all their influence against, not for, the exaction of a great indemnity from Germany."

Financial influence against War Indemnity.

Even supposing, that, to avoid the patent folly of such a sudden operation, the payment of the indemnity were spread over some years, the dislocation of world finance and a particular

injury to the finance and business of England would ensue, while the heavy taxation which Germany would be obliged to impose upon her people would cripple her power as a large customer of British goods, retard her industrial development, thus reducing her supply of the goods our people wanted to buy from her, and would prevent her from applying her share of capital in opening up South America and other countries whose development is so beneficial to our commerce and our investments.

Increased taxation for War Indemnity purposes.

Every decade the linkage of financial and commercial interests across political frontiers grows so much stronger and more complex that the direct material recoil of war becomes graver and more obvious. Nations in the modern business world cannot, any more than individuals, live to themselves alone. Modern finance is the great sympathetic system in an economic organism in which political divisions are of constantly diminishing importance. Of course, so long as governments, and the public force and money which they handle, can be utilized by private syndicates, either to procure profitable concessions or to improve the marketable value or the yield of properties in foreign lands, the political factor will be liable to be introduced in emergencies. Investors, like traders, will tend to group themselves on such occasions under their flag, striving to cover their profit-seeking deals under some cloak of national policy. But so far as the relations of the civilized powers with one another

Tendency of Modern Finance towards Peace.

are concerned, the growing community of business interests, which the international web of finance involves, is the most solid pledge and the aptest instrument for the preservation of peace.

Increasing cost of War an assurance of greater Peace.

It will, no doubt, be justly said that our argument assumes for its full efficacy a larger measure of reason and of calculated policy than history discloses in any nation, that nations goaded to fury by some insult or deluded by some reckless statesman, may throw the plainest dictates of self-interest to the wind, risking all the damages which we have enumerated. But as the cost of war increases, there is good evidence that nations are more apt to count it. The appalling ruin which a war between great European powers would bring, not only to the participants, but to the bystanding nations entangled by innumerable bonds of business with one or other of the combatants, is sufficiently well realised by the solid business classes in every nation to yield a very potent public feeling against war. It is this reasonable caution that, far more than any humanity or timidity, has given, through The Hague Conventions and the growing use of arbitration, substance to what, a generation since, were but vague and pious aspirations of philanthropists.

Consolidation of Financial Interests opposed to Warfare.

That which Christianity, justice, and humane sentiment have been impotent to accomplish through nineteen centuries of amiable effort, the growing consolidation of financial interests, through bourses, loans, companies, and the other machinery of investment, seems likely within a

generation or two to bring to consummation, namely, the provision of such a measure of effective international government as shall render wars between great civilised powers in the future virtually impossible.

Not merely a handful of great financiers and merchants have important interests in other countries whose safety and prosperity they therefore prize. Thousands of middling citizens, manufacturers, tradesmen, professional men, even clerks and employees, in England, Germany, United States, or France, have interests, as owners of securities, in the welfare of one another's country. A rupture between any two of these countries would come home at once to active business men in every city or town of Great Britain or of Germany as a damage to their outlying properties. For modern international finance means that Germany, as an economic asset, does not belong entirely to the Germans, but that parts of it belong to Britons, while parts of Britain, on the other hand, belong to Germans. Both, moreover, are largely interested in securities in other countries, all of which are liable to suffer damage if Germany and Britain quarrelled with one another, or failed to exert their joint influence to bring other quarrelling nations to a pacific settlement of their disputes. What applies to the case of Germany and Great Britain applies, of course, with varying degrees of intensity to the relations of other powers. In one or two

Cosmopolitan character of Foreign Investors.

Pacific qualities of International Investment.

instances, as that of France and Russia, the direct financial bonds are so tight as to make a rupture incredible.

The hostile element in Finance in the minority.

But everywhere the growth of a network of direct and indirect financial interdependency offers a considerable guarantee for peace. There will doubtless remain subordinate, though not inconsiderable, monetary interests which feed international hostility, financing debts for military and naval equipment, sustaining the shipbuilding, gunmaking, and other industries which live on profitable government contracts for armaments, or seeking speculative profits through the violent oscillations of credit brought about by strains of international relations. But, perilous as is this play of interested or reckless finance, it has less power than is sometimes ascribed to it. For even those interests which thrive on armaments and international unsettlement would generally be losers by actual war, and will help to pull up on the brink of such a precipice. The main current of finance, drawing its sustenance from the security and productiveness of transport, industrial operations and material development of civilised life in the various countries of the world, demands peace and stability of government as first conditions of its free and profitable flow. War, fear of war, and political unsettlement, on the one hand, retard the growth of surplus wealth out of which savings can be made, checking the stimulus to create capital, upon the other, limit the areas of profitable investment, and reduce the efficiency of the work of world-development which international finance exists to carry on.

Investors' need of efficient Government.

CHAPTER VIII

THE PROBABLE FUTURE OF INVESTMENT.

THE present value of all stocks and bonds depends so much upon what is likely to happen in the future to the governmental or economic undertakings which have absorbed the capital and have promised to pay interest, that every intelligent investor must be so far a "speculator" that, in making or maintaining an investment, he seeks to forecast the economic future as it affects his investments.

Economic future of Investments.

If he is considering the purchase of railroad shares in a British company, he will, if he is prudent, not merely confine his view to a cursory examination of the recent fluctuations in the prices of such shares, on the presumption that they reflect quite accurately the expert expectations of the future earning-power of railway capital. He will bring his own judgment to bear upon certain important considerations that are likely to affect the value of railway capital in the near future, such as the competition of tramways and other modes of transport, the probable necessity of large capital outlays in electrification,

Future value of British railroad shares.

the rising wage-bills, the probable rises in price of coal, the possibilities of state purchase and of the terms on which such purchase would be likely to take place. These and many other factors should help to determine what shares he should buy and what price he should be willing to pay or to accept.

Mining and Rubber Shares.

If it is a mining or a rubber company whose shares are in question, even the most reliable statement of present relevant facts, could he obtain them, would not suffice. He needs to know not merely the size, shape, direction, richness of the reef, the costs of working and the market price of the product, etc., for the mine, the size of the estate, number and yield of trees, supplementary products, supply of labour, etc., for the rubber company. Granted that he is dealing with a genuine proposition and that all present accessible facts are fully disclosed (a large assumption !), he would still require to consider whether the price at which the shares were offered adequately discounted risks relating to the future of the mining or the rubber industries. For instance, whether the rapid development of other rich mines were likely to bring down perceptibly the price of the gold, or whether changes of habits might not affect diamonds, whether cheaper compositions were likely to be substituted for rubber. Every current price of any shares does of course to some extent reflect all such contingencies, but every intelligent investor will apply his private

Careful investigation of future probabilities.

judgment to considering whether the market reflection is accurate and adequate.

Economic occurrences in the future of Capital Productivity.

The number of economic happenings in the future which must affect the productivity of any sort of capital, and which, therefore, could they be foreseen, would affect present prices, is absolutely infinite. As a rule, those concerned with some particular class of stocks, e.g., British rails or Kaffirs, only take into some account important special tendencies affecting these uses of capital. They are apt, perhaps from the inevitable focus of such undertakings, to ignore, or take no real account of, larger economic movements which affect the probable future of whole classes or whole areas of investment, or indeed of the art of investment as a whole. Even those who have the intelligence to apply to their investment the general economy of wide geographical distribution do not bring sufficient thought, as a rule, to the forces and facts that underlie and give efficacy to this economy.

Economy of Distribution of Investments.

It has in effect two bases, one relating directly to physical conditions, the other consisting of a complex of economic-historical conditions partially but not always closely dependent upon the first. Let us take the exact statement of the economy of Distribution of Investments as given by Mr. Lowenfeld* :—

> If an investor divides his capital equally among a number of stocks, every one of which

* "Investment an Exact Science," p. 51.

is under a different trade influence, then each of these divisions of his capital will constitute a distinct investment risk, and a true system of averaging investment risks is thereby established.

Economy of Investment risk.

Now the truth of this general statement of economy of risk is absolute and undeniable. But to what extent does difference of trade influence correspond with difference of geographical areas? To what extent do all the stocks of capital in a particular country or geographical area vary directly with one another and reversely in direction or in extent with the stocks in another geographical area? Are there certain kinds of stocks, e.g., government bonds, railroad securities, or industrials, which obey the geographical law more closely or less closely than others? Are there, again, certain diverse geographical areas the stocks of which tend to move in some close sympathy, as if some other conditions were more potent than those of geographical division?

Tendency of Stocks in a particular Geographical Area to move in unison.

Adequate answers to such questions could only be furnished by means of a detailed comparative study of large classes of securities in different geographical areas for a considerable number of years, a statistical enquiry which would involve great labour. Concerned as we are here with broader principles of the art of investment, it must suffice to indicate some lines of reflection based upon our economic interpretation of financial tendencies. Similarity of physical conditions i.e., climate, geological formation with related

flora and fauna, situation with regard to other countries and natural facilities of access, will form a strong basis of unity of "trade-influence" in respect of capitalistic development and financial fluctuations. Countries in close proximity to one another, or on the same latitude, will have certain important economic attributes in commerce, their organic life, animal and vegetable, inclusive of man, will exhibit similarities which will contribute to a similarity of industrial development. Not less important than this natural similarity will be the imitative and interactive influences which will lead men living in the same part of the world to evolve similar modes of work and of life, again conducing to similarity of economic structure.

In explanation of Similarity in Price Movement.

Such obvious considerations would support a *prima facie* case for supposing that the economic fortunes of neighbouring countries will resemble one another in their rises and falls, and that important events, natural or political, will affect for good or evil, simultaneously, all the forms of capitalistic enterprise in one of these areas. The simplest example, of course, is a drought or a crop disease affecting the staple industries of a group of neighbouring lands, or some great labour trouble or political disturbance, paralysing the trade and creating a general feeling of insecurity over a continent. It is easy to recognise that any such misfortune will affect injuriously all the industries and the entire credit structure of a country or a set of countries in the same part of the world. Neighbouring lands, again, with

Causes of sympathy in price fluctuations.

similar natural resources and racial affinities in their population, will tend to evolve in civilisation, not merely along the same lines, but approximately at the same place, so that their current history will present considerable resemblances. While property will be relatively secure in all the Western European countries, political corruption and revolutionary violence will be rife in most South American states, and infections of feeling will give a certain simultaneity of disturbances. It is the presumption that natural conditions and human history in their economic bearings will be much the same in neighbouring portions of the earth that gives general validity to the law of Geographical Distribution of Investments. But it deserves attention that, in the scheme of this distribution, geographical conditions are not always paramount. British colonies, for example, are placed in a class by themselves, though their affinity is not geographical but political; e.g., Canada stands not, as it might, geographically, with the United States, but with the other self-governing colonies. This is, perhaps, a justifiable exception, for though strong. natural and cultural features are common to the United States and Canada, the British imperial connection is probably at present a more potent cause of credit fluctuations. But its presence in the scheme serves to indicate that, for purposes of risk calculation, in the art of investment, geography is not always the dominant factor.

Validity of the law of Geographical Distribution of Investments.

Position of Canada in Geographical Distribution of Investments.

Regarded as investment areas, from the stand-

point of security and yield, the various countries will really rank more according to the level of material and moral civilisation they have reached than by any other basis of comparison. Geography will, of course, be of prime importance in the sense that, both industrially and financially, close sympathy exists between the different undertakings in the same country, and that some measure of this sympathy extends among neighbouring countries. There is, however, no reason to suppose that industrial investments in East Prussia will move in sympathy with industrial investments in West Russia, or even that Japanese and Chinese investments will show similar wave-movements.

Relation of Countries in Geographical Distribution of Investments.

At present, nationality and political movements on a national scale pay so important a part in causing fluctuations of credit that they probably furnish a better basis of classification for investments than does the use to which the capital is put. But as internationalism in finance becomes more effective, the geographical and political basis of classification may probably come to be displaced in large measure by an economic basis, by which investments will be graded for security or yield more by the economic function served by the capital.

Economic basis in Investment classification.

If all important nations attained settled modes of government, with little chance of war or revolution and with equally intelligent and profitable uses for their borrowed money, the security and yield of government bonds all over the world

would tend to stand upon a level and to vary in the same directions, though geographical considerations might still exert some influence. Railway investments over large portions of the world, when the main roads have been fully equipped, may vary in value more for reasons common to all countries, as, for instance, the growth of road motor traffic, than for reasons expressly related to other economic happenings in their particular area.

International Investments on the Increase.

Assuming the general accuracy of our prognosis, based upon the study of current tendencies, viz., that international will continue to gain upon purely national finance, and that this will help to secure peace and order over all areas of international investment, it is possible to make some rough sort of speculative forecast of the financial future. Such a standardisation of order throughout the world, the financial and commercial interest in peace, perhaps supported by an international code and police, would have a most stimulative effect upon the art of investment.

The Loadstone to natural economy of Investment.

For it is political and legal insecurity, and the related risks, that hitherto have thwarted what may be termed the natural economy of investment, the tendency of capital created at any point to flow freely over the surface of the globe in search of the place and mode of most productive employment. Once establish a tolerably effective international security of property over the civilised world, there will ensue an immense development of joint-stock capital and great

economies in its profitable use. The freer flow of capital from the developed industrial areas, where there is a large surplus in excess of local needs, into the backward areas, would stimulate the pace of development in the latter, enabling them more quickly to reach the stage in which they could themselves contribute to the current of investment. For, though every new area fertilised by foreign capital may at first be drained of its surplus to pay the interest and dividends upon its loans, when its development upon a basis of solid natural resources and labour is once secure, the business men upon the spot obtain an ever increasing measure of ownership and control, and soon become large contributors to capital.

How minor states become contributors to Capital.

The history of the United States is, of course, the largest illustration in recent times. Its railroad and, in large measure, its industrial development after the Civil War was financed by foreign, mainly British, capital. But as the development of the West advanced, though British capital continued to flow in, the proportion of home-made savings grew until the United States has reached a stage in which her capital not merely supplies the great share of her own demands but is beginning to seek large outside markets for investment. Canada has now attained the position which the United States held a couple of generations ago. But as both the credit system and the mechanism of immigration are more highly evolved than in last century, the economic evolution of Canada will be proportionately accelerated, moving swiftly

Growth of United States Finances.

towards a time when she will have a large surplus for saving and investment beyond the fund for paying dividends to foreign investors. But if the United States, and then Canada, thus pass from the stage of debtor into that of debtor plus creditor nations, and if one by one the other great areas for our foreign investments, Argentina, Brazil, South Africa, Mexico, Australasia, Japan, even India, Russia, and China, pass through the same phases, themselves becoming in their turn great feeders of the stream of joint-stock capital, what will be the future of investment from the standpoint of the yield of capital? Can the economic system of the world usefully absorb and apply productively the apparently illimitable supply of fresh capital that would be forthcoming under such conditions as we describe?

Progress of the Powers in supply of Joint-Stock Capital.

Though we are at present so far removed from the condition of the world here indicated that in each of the great areas just named a vast amount of developmental work still seems to call for foreign capital, the keen rivalry between foreign syndicates to do this work appears to indicate that for certain profitable areas, at any rate, an actual or potential excess of capital already exists. Whenever trade is good and public confidence strong, it appears possible to attract to any great developmental work, conducted either by a state or by private enterprise, more capital than is required. If then more nations reach the stage attained by the United States when the balance of indebtedness turns from the debit to the credit

Excess of Capital in certain Investment Areas.

side, developed industries supplying funds of saving for investment abroad, it looks as if a permanent excess of capital might bring down interest to a merely nominal amount. A larger number of nations, with larger capacities of saving beyond their own urgent needs of capital, would seem to be confronted by a smaller number of profitable areas of external investment. Moreover, it might appear as if, when the most fundamental work of capital is substantially completed, the world being fairly well equipped with railroads, harbours, docks, and the more important forms of municipal plant, further supplies of capital must seek employment more largely in work essentially more irregular and risky. For it appears inevitable that an increased proportionate flow of capital into manufacturing and commercial businesses, or into other companies for furnishing special utilities and enjoyments to consumers, will involve greater risks, both in regard to the safety of the capital and the reliability of its yield. The quantity of foreign capital that goes into industrials is at present a very small percentage, largely from a just instinct for avoiding securities so largely dependent upon factors both of cost and of market which demand special local knowledge for their appraisal.

The Problem of an over-supply of Capital.

Small percentage of Capital employed in Industries.

But before we assent to these apprehensions regarding the excess of capital and the growing risks of investment in the future, several more reassuring possibilities deserve consideration. As the swift rise of the great motor industry and the

still more recent experiments in aviation testify, the age of inventions shows no signs of passing. On the contrary, the expansion of scientific and technical training and the increased co-operation of inventive minds throughout the world would indicate a constant acceleration of the pace at which the physical sciences can be made to serve the purposes of man. Mechanics, physics, chemistry, biology will by their advances probably impose great adaptations of structure and of function even in our fundamental industries of transport, while the reconstruction of our cities to fulfil the needs of more enlightened men will play an even larger part in the next generation than in the past. Though, therefore, many of those capitalistic industries which will come into being to supply by manufacture the specialised needs of bodies of consumers may very likely play a more important part than now in the markets for investments, an immense quantity of what we term developmental work will also be continually going on.

Fresh channels for Capital Investment.

The questions whether the pace of saving will be such as to yield excesses of capital, and whether, by large recourse to essentially more precarious employments, investment will become less secure, depend for their answer, however, very largely upon the forecast we make of the social-economic condition of society in the civilised countries of the world.

The doubt regarding future Security of Capital.

There are three principal economic conditions essential to the full application of the art of joint-

stock investment as the instrument enabling savings to function most securely and most productively. Upon the extent to which these conditions are fulfilled the future of financial capitalism chiefly depends.

Capital and the Labour Question.

The first is freedom and facility of immigration. Capital cannot do its economic work without labour. It cannot rely upon the presence of an adequate amount of suitable native labour being available for use whenever it is wanted. The making of a great trunk railway, or a Panama Canal, the operation of Transvaal gold mines, or of sugar plantations in Queensland, however useful and profitable such enterprises may be, are impracticable unless the flow of capital is able to induce a corresponding flow of labour from external sources of supply. For, though in some cases native labour may be readily procurable for working a railroad, a mine, or a manufacture, once established, it almost always requires the help of external supplies for the initial work of development. Unless, therefore, the effective fluidity of labour corresponds to that of capital, there is evidently a waste of productive power.

Necessity of external labour supply.

Now, though it is not very much more costly to carry workers than to carry the products of labour, the actual capital, in the shape of machinery, materials, etc., Adam Smith's dictum nevertheless remains true that "a man is of all sorts of luggage the most difficult to be transported." For he is not absolutely "economic," in the sense of responding at once and proportionately to the

cash inducement which capital may offer in the shape of pay. He has certain attachments of a non-economic nature which fasten him with more or less of fixity to his native land. Even when he moves he does so with less freedom than is the case with capital; he can be induced to go to certain places for a certain time on certain conditions.

Independence of the workman.

This fact is, of course, quite consistent with the statement that for sufficient money enough labour of any kind can be got for service anywhere. In every nation there are adventurous men who move with tolerable facility along the line of maximum remuneration. There are certain races who in recent times furnish a fund of international labour available in large numbers for work in any part of the world. Italians are found roadmaking all over Central Europe and North and Central America, and large areas of fluid labour are being opened up in Austro-Hungary and the neighbouring Slavonic countries. Malays and Chinese are able and willing to adapt themselves to a great variety of climatic and other conditions. As international intercourse grows closer it would seem likely that the supply of fluid labour of various types procurable for co-operation with capital, anywhere where profitable opportunities of investments were disclosed, would increase rapidly. And this would certainly tend to be the case if distinctively economic forces were allowed free play. But they are not. Political, racial, linguistic, and other divergencies express them-

The co-operation of Capital and Labour.

selves in obstructions to free movements of populations. Even where personal violence is not resorted to, an intricate and effective social and economic boycott retards the immigration of unwelcome strangers.

Social and Economic boycott of Immigration.

But this barrier is usually strengthened by political restrictions and disabilities, frequently by a rigid policy of prohibition. It is not advisable, or indeed, possible, here to enter on a discussion of the "pros" and "cons" of this policy which has been adopted by some of the most civilised nations in the world upon grounds, partly racial, partly social, partly economic. It must suffice to recognise that these legal restrictions upon free immigration sharply contravene the economy of modern financial capitalism. This is made especially manifest from the fact that the restrictions are particularly directed against the entrance of races or classes of labour considerably cheaper than the labour inside the country. Though the grave possible reactions upon social order, and the indirect damage to the efficiency and progress of the working classes from exposure to an unchecked influx of cheap foreigners, may turn the scale in favour of regulations, when a wider view of social economy is taken, it is evident that this policy imposes a very real restraint upon the present freedom of financial enterprise.

Restricted immigration an obstruction to Financial Enterprise.

Similarly, all interferences with freedom of exchange of goods and services, by tariffs, bounties, navigation laws, or other restraints, impede

the tendency of capital to seek the most productive employments. For since all foreign investments are effected in the first instance by means of exports, the restraints upon free importation which a protective policy imposes operate as a restraint upon freedom of investment. Though some foreign capital may be tempted into a protected country in order to share the artificially stimulated prosperity of some particular protected industry, the nett effect is to keep out foreign capital. Thus nationalism in industry and commerce involves nationalism in saving and investment as distinguished from internationalism. Here, again, I am not concerned to adjudge the merits of this protective policy, which may be able to defend itself, either by regard to a longer time-focus of economic interests, or by wider considerations of national polity. For this analysis it is enough to realise that so far as a tariff or other protective policy keeps out foreign goods, it limits freedom of international investment and reduces the average productivity and yield of capital.

Protection a bar to freedom of Investment.

Finally, the future of investment as regards (1) the growth of volume of employment for capital, and (2) the security and regularity of yield for capital, depends upon the distribution of incomes and consuming power among the various nations and classes that comprise the industrial world.

Future of Investment dependent on the Industrial World.

It is often supposed by members of the "propertied" classes that the movements everywhere on foot among the working classes to raise wages

and to secure for labour a larger share of the wealth of the country or of the world, of necessity involves an injury to the interests of capital. This conclusion is natural enough for a business man who looks at the immediate particular effect of a rise of wages extorted by a trade union in his local industry. Though within certain limits the "economy of high wages" may operate so as to raise the efficiency of labour to correspond with the rise of wages, thus cancelling the damage to profits that was anticipated, this cannot be regarded as a necessary result. If, as is reasonably held, the nett result of the operation of public opinion, collective bargaining, and legal intervention on behalf of labour, is to raise the proportion of the general product of industry that goes in wages, this will imply a diminution in the proportion that goes in rent, profits, and salaries.

"Economy of high wages."

Since the greater part of the savings that go to sustain and enhance the capitalist structure undoubtedly proceeds from these latter sources of income, it might appear that any diminution in their share of the total wealth must be attended by a reduction in the volume of investment. But this supposition is unwarranted. I have more than once referred to the fact, familiar to all business men, that it is usually much easier to buy than to sell, the industrial system, as a whole, appearing to contain a producing power in excess of the current requirements of consumers as expressed through demand for commodities. What applies to markets for produce, applies likewise

Industrial Supply in excess of Demand.

to the investment market. Excepting on the morrow of some great shock to credit, more capital than is wanted seems to be available for every reasonably safe and profitable project, and for many which are neither safe nor profitable. Wherever the investment business is open to free competition, the keenness of the struggle between rival groups and syndicates of financiers attests the existence of a superabundance of available capital.

Abundant Capital in readiness for Investment.

If it be objected that much of this "capital" never materialises and could not, consisting largely in speculative undertakings to find money, the whole of which could not be found, a more solid test may be applied. It has been already shown that every period of trade depression is full of concrete evidence of an excess of actual industrial capital, indicating the continuous tendency of the industrial system to create and to seek to operate a large quantity of plant and other concrete capital than can or does obtain full regular employment. Though, according to older economic theory, there can be no general over-production, because goods ultimately exchange against goods, and (the wants of man being infinite) whatever is produced will induce some one to consume it, the business man knows that industry does not work out in this simple satisfactory manner. He is aware that the rise in consumption does not in fact keep pace automatically with the rise in production, but normally tends to lag behind. The necessary result of this

Tendency of excess of Capital in time of Trade Depression.

failure fully to raise the volume of consumption of commodities, so as to furnish full and regular employment to capital and labour, is to limit needlessly the quantity of new capital which can find profitable employment through investment. When once this tolerably obvious economic truth is grasped, it becomes evident that an improvement in the wage-standards of labour, leading to a general rise in the standard of consumption of the working classes, who form the great majority of the population in every land, would involve an increased use of capital. So far, then, from inflicting injury upon capital, a strengthening of the consumption of the masses would operate as a demand for more capital. Nor is that the only benefit which would accrue from a more equal distribution of wealth. A rising standard of working class consumption will not merely enhance the volume of employment for capital and labour, it will tend to abate the fluctuations which occur at present. For by increasing the proportion of the general income expended upon those necessaries and conveniences of life which form the conservative part of expenditure, and correspondingly reducing the proportion spent on the more capricious forms of demand, an increased steadiness will be imparted to the working of the industrial system as a whole.

Effect on Capital of increased consumption of commodities.

Increased stability in the working of the Industrial System.

The apparent paradox that an improvement of wages which appears to be made at the expense of capital really involves a larger and a more regular demand for capital, disappears when it is

recognised that the more equal distribution of wealth stimulates a larger aggregate volume of production. More capital will be wanted and used to sustain the larger volume of production and consumption.

Social progress beneficial to Joint-Stock Capitalism.

Though the particular methods of conflict employed to secure increases of wages are sometimes fraught with injury and waste, the future of investment stands to gain and not to lose by a distribution of wealth that secures a larger share to the workers who will apply their increased spending power in a demand for commodities. Social progress, conducted with peace and regularity along these lines, conduces to throw a continually increasing number of large staple industries into the condition favourable to the operation of joint-stock capitalism. Even if, as is probable enough, the present forces, making for an increase of state and municipal enterprise, should absorb some of these industries, converting them from private into public businesses, this is not of necessity adverse to the interest of future investors. Of course, if public bodies show themselves incompetent for business management, they will waste capital, and the damage to society as an economic system may be considerable. But unless this "socialism" were carried to such reckless extremes, as to wreck the credit of the State, the conversion of private stock-holders into public fund-holders is not an injury to the art of investment. For other things equal, a public stock in a creditable state or municipality is a

Incompetent business management a Menace to an Economic System.

more secure investment than most private stocks, having for its guarantee the whole taxing power of the State. However, no general argument for extension of public enterprise can be derived from this statement. For unless the nett economy of public undertakings can be brought fairly on to the level of economy of private companies engaged in similar work, the preference of the former method would imply a nett reduction in the production of capital as an aggregate. From the standpoint of public welfare, which has regard to other matters besides profit, this will not, of course, be a final ground for condemnation. But in our interpretation of investment as an economic process, a presumption will always lie in favour of such freedom of competition between the various modes and channels of investment as shall carry capital in sufficient quantities to every quarter of the industrial world where it can help in the production of wealth.

Private Companies v. Public Companies.

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